

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA

DOCKET NO. 2000-207-W/S – ORDER NO. 2001-887

AUGUST 27, 2001

IN RE: Application of Carolina Water Service, Inc. for Approval) ORDER
of an Increase in its Rates for Water for all its Service) RULING ON
Areas and Sewer Service for Certain of its Service Areas.) APPLICATION
) FOR INCREASE
) IN RATES

I. INTRODUCTION

This matter is before the Public Service Commission of South Carolina (the “Commission”) on the Application of Carolina Water Service, Inc. (“CWS” or the “Company”), filed on February 23, 2001, seeking approval of a new schedule of rates and charges for water and sewer service that CWS provides to its customers within its authorized service areas in South Carolina. The Application was filed pursuant to S.C. Code Ann. Section 58-5-210 *et seq.* (1976), as amended, and 26 S.C. Regs. 103-821 (1976).

By letter dated March 20, 2001, the Commission’s Executive Director instructed CWS to publish a prepared Notice of Filing, one time, in newspapers of general circulation in the areas affected by CWS’s Application. The Notice of Filing indicated the nature of the Application and advised all interested persons desiring to participate in the scheduled proceedings of the manner and time in which to file appropriate pleadings for inclusion in the proceedings. In the letter of March 20, 2001, the Executive Director also instructed CWS to notify directly, by U.S. Mail, each customer affected by the

Application by mailing each customer a copy of the Notice of Filing. CWS furnished the Commission with Affidavits of Publication and an Affidavit of Mailing demonstrating that the Notice of Filing had been duly published and mailed to all customers affected by the Application in accordance with the instructions of the Executive Director. In response to the Notice of Filing, Petitions to Intervene were filed on behalf of Philip S. Porter, Consumer Advocate for the State of South Carolina (the “Consumer Advocate”), River Hills Community Association, Inc. (“RHCA”), and the South Carolina Department of Health and Environmental Control (“DHEC”).¹ A Petition to Intervene Out of Time, “filed” by a customer of CWS, was denied intervention in the proceedings.²

S.C. Code Ann. Section 58-3-95 (Supp.2000) provides in relevant part that “[w]hen a corporation or person furnishing ... water, sewerage collection, sewerage disposal, ... files a schedule setting forth proposed changes with the Commission pursuant to the procedures prescribed in this title, a panel of three members of the Commission shall hear and rule on the proposed changes.” Pursuant to S.C. Code Ann §58-3-95 (Supp.2000), the Chairman of the Commission appointed the panel to hear and rule on CWS’s Application. The panel consisted of Chairman Saunders, presiding, Commissioner Carruth, and Commissioner Atkins.

¹ By letter dated May 29, 2001, DHEC requested leave to withdraw its Petition to Intervene, and DHEC’s request to withdraw its Petition to Intervene was approved by Commission Order No. 2001-536, dated June 4, 2001.

² On June 11, 2001, the Commission received a Petition to Intervene Out of Time from Brenda W. Bryant, a customer of CWS. By Order No. 2001-633, dated July 2, 2001, the Commission denied the Petition to Intervene Out of Time.

In addition to the scheduled hearing during normal Commission hours, the Commission held three public night hearings.³ On June 18, 2001, the Commission held a night hearing in Lake Wylie, South Carolina. On June 25, 2001, the Commission held a night hearing in the Commission's hearing room located at the Commission's offices in Columbia, and on July 9, 2001, the Commission held a night hearing in Summerville, South Carolina. On July 11, 2001, the public hearing relative to the matters asserted in CWS's Application was commenced in the Commission's hearing room located at, Synergy Business Park, 101 Executive Center Drive – Saluda Building, Columbia, South Carolina. The public hearing was not completed on July 11, 2001, and was reconvened and concluded on August 6, 2001.

During the proceedings, CWS was represented by John M.S. Hoefer, Esquire. The Consumer Advocate was represented by Elliott F. Elam, Jr., Esquire. RHCA was represented by Scott Elliot, Esquire. The Commission Staff was represented by Florence P. Belser, Deputy General Counsel and Jocelyn G. Boyd, Staff Attorney.

At the night hearings and at the public hearing on July 11, customers of CWS presented testimony to the Commission concerning their views of the requested rates and experiences with the Company's service. At the hearings on July 11 and August 6, the Company presented the testimony of Carl J. Wenz, Vice President Regulatory Matters of Utilities, Inc.⁴; Pauline M. Ahern, Vice President of AUS Consultants – Utility Services; Carl Daniel, Group Vice President and Regional Director of Operations for CWS; and

³ The purpose of the night hearings was to provide a forum, at a convenient time and location, for customers of CWS to present their comments regarding the service and rates of CWS. The hearings were scheduled in areas where CWS provides service and where the customers had requested a public forum.

⁴ Utilities, Inc. is the parent company of CWS.

Samuel B. Davis, Regional Manager for CWS in Lexington and Richland Counties. The Consumer Advocate presented the testimony of Michael A. Bleiweis of The Woodside Group, Inc. and John B. Legler, a private consultant specializing in utility finance. RHCA presented the testimony of W. Robert Harrington, a member of the Utilities Committee of RHCA. The Commission Staff presented the testimony of Sharon G. Scott, an Auditor for the Public Service Commission of South Carolina; William O. Richardson, an Engineer Associate with the Public Service Commission of South Carolina; and James E. Spearman, Research & Planning Administrator for the Public Service Commission of South Carolina.

In considering the Application of CWS, the Commission must consider competing interests. The interests of the consumers to receive quality service and a quality product at a reasonable rate compete with the interests of the provider to have the opportunity to earn a fair rate of return. Regulation, as it has developed in the United States, is concerned with rates, service, [and] safety Charles F. Phillips, Jr., *The Regulation of Public Utilities*, (1993) at 171. Rate regulation has two aspects: control of the rate level (earnings) and control of the rate structure (prices). *Id.* As to the rate level, public utilities are entitled to cover all allowable operating costs and to have the opportunity to earn a “fair” rate of return. *Id.* Collectively, these items comprise a company’s total revenue requirements. *Id.* As to the rate structure, public utilities are permitted to establish rates that, at a minimum, will cover their revenue requirements. *Id.* at 171-72. Such rates must be “just and reasonable,” with no “undue” discrimination. *Id.* at 172.

Thus, in considering the Application of CWS, the Commission must give due consideration to the Company's total revenue requirements, comprised of allowable operating costs and the opportunity to earn a fair rate of return. To this end, the Commission will review the operating revenues and operating expenses of CWS and will endeavor to establish adequate and reasonable levels of revenues and expenses. Further, the Commission will consider a fair rate of return for CWS based upon the record before it. Should the Commission's determination show that rates should be increased, the Commission will then design rates that will meet the revenue requirements of CWS but that are also just and reasonable and free of undue discrimination.

One procedural matter must be resolved by the Commission. During the hearing, counsel for CWS moved to strike a portion of RHCA witness Harrington's prefiled testimony. The Motion to Strike covered witness Harrington's testimony from page 4, line 14 to page 5, line 8 and Exhibits B and C attached to Harrington's testimony. The stated grounds for the Motion to Strike were hearsay. Harrington's testimony, which is the subject of the Motion to Strike, discusses residential growth in the Lake Wylie area of York County. We held the Motion to Strike in abeyance during the hearing.

After reviewing Mr. Harrington's testimony, the Motion to Strike is denied. Mr. Harrington is a resident of the River Hills Community in the Lake Wylie area and therefore he could very well be knowledgeable about the residential growth in the Lake Wylie area. Additionally, Mr. Harrington has been a member of the York County Planning Commission since July 1999. The duties and responsibilities of the York County Planning Commission are to review and approve all development in York County

based upon the existing land use plan developed by the Planning Staff. Harrington Direct Prefiled Testimony, p. 1. As a member of the York County Planning Commission, Mr. Harrington testified that he, in conjunction with other members of the Planning Commission, approve all development in York County, including the CWS territory. Mr. Harrington also previously served on the York County Zoning Board of Appeals. As an obviously active member of his community, Mr. Harrington has personal knowledge regarding residential growth that has taken place in the past and expected residential growth expected to take place in the future. As we have ruled that Mr. Harrington's testimony is not hearsay, we will assign the appropriate weight and credibility to Mr. Harrington's testimony that we believe is appropriate. *See South Carolina Cable Television Ass'n v. Southern Bell Tel. and Tel. Co.*, 417 S.E. 2d 586, 589 (1992) (holding the weight and credibility assigned to evidence presented is a matter peculiarly within the province of the PSC).

II. FINDINGS OF FACT

1. CWS is a water and sewer utility providing water and sewer service in its assigned service areas within South Carolina, and its operations in South Carolina are subject to the jurisdiction of the Commission, pursuant to S.C. Code Ann. § 58-5-10, *et seq.* (1976), as amended.

2. The appropriate test year period for the purposes of this proceeding is the twelve-month period ending December 31, 2000.

3. The Commission will use rate of return on rate base as a guide in determining the lawfulness of the Company's rates and in the fixing of just and reasonable rates.

4. The determination of return on rate base requires three components. These three components are capital structure, cost of equity (or return on equity), and the cost of debt.

5. In the return on rate base determination, it is appropriate to use the capital structure and cost of debt of CWS's parent company, Utilities, Inc. at December 31, 2000. The capital structure for Utilities, Inc. at December 31, 2000, is 50.09% long-term debt and 49.91% equity, and the cost of debt of Utilities, Inc. at December 31, 2000, is 8.62%.

6. A fair return on equity for CWS is 11.50%.

7. Using the capital structure of Utilities, Inc. at December 31, 2000, of 50.09% long-term debt and 49.91% equity; the cost of debt of Utilities, Inc. at December 31, 2000, of 8.62%; and a return on equity of 11.50%, produces a rate of return on rate base of 10.06%.

8. By its Application, CWS is seeking an increase in its rates and charges for water and sewer service which results in \$685,063 of additional revenues to CWS.

9. The appropriate operating revenues for CWS for the test year under present rates and after accounting and pro forma adjustments are \$4,891,487.

10. The appropriate operating expenses for CWS for the test year under present rates and after accounting and pro forma adjustments and adjustments for known and measurable out-of test-year occurrences are \$4,012,749.

11. The appropriate rate base for CWS for the test year after accounting and pro forma adjustments and adjustments for known and measurable occurrences outside the test year is \$11,464,268.

12. A customer growth adjustment using the method for calculating customer growth as proposed by the Staff is appropriately included in computing the income requirements of CWS.

13. The income requirement for CWS, using the return on rate base of 10.06% found appropriate in this Order and the adjusted rate base of \$11,464,268, is \$1,153,275.

14. In order for CWS to have the opportunity to earn its income requirement of \$1,153,275, CWS must be allowed additional revenues totaling \$406,246.

15. In designing rates for CWS, a uniform rate schedule for the base facility charge for water customers is appropriate. Further, the sewer rates shall not be increased for customers in Lincolnshire service area, I-20 service area, Lexington service area, Kings Grant service area, and Teal on the Ashley service area.

16. The appropriate operating margin for CWS based upon the herein approved adjustments and rates is 12.43%.

III. EVIDENCE AND CONCLUSIONS

In this section, the Commission sets forth the evidence relied upon in making its Findings of Fact as set forth in Section II of this Order.

1. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 1

The evidence supporting this finding concerning the Company's business and legal status is contained in the Application filed by CWS and in prior Commission Orders in the docket files of the Commission, of which the Commission takes judicial notice. This finding of fact is essentially informational, procedural, and jurisdictional in nature, and the matters which it involves are not contested by any party.

2. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 2

The evidence supporting this finding, that the appropriate test year period for the purposes of this proceeding is the twelve-month period ending December 31, 2000, is contained in the Application filed by CWS and in the testimony and exhibits of the parties' witnesses.

On February 23, 2001, CWS filed its Application requesting approval of the rate schedules designed to produce an increase in gross revenues of \$685,063. CWS's Application was based on a test period consisting of the twelve-months ending December 31, 2000. The Staff and the Consumer Advocate likewise offered their evidence generally within the context of the same test period.

A fundamental principle of the ratemaking process is the establishment of a test year period. In *Heater of Seabrook v. Public Service Commission of South Carolina*, 324 S.C. 56, 478 S.E.2d 826 (1996), the Supreme Court of South Carolina noted that "[t]he 'test year' concept is very important in the rate-setting process. In order to determine what a utility's expenses and revenues are for purposes of determining the reasonableness of a rate, one must select a 'test year' for the measurement of the expenses and revenues."

478 S.E.2d 828 n.1 (1996). The test year is established to provide a basis for making the most accurate forecast of the utility's rate base, reserves, and expenses in the near future when the prescribed rates are in effect. *Porter v. South Carolina Public Service Commission*, 328 S.C. 222, 493 S.E.2d 92 (1997), citing *Hamm v. S.C. Pub. Serv. Comm'n*, 309 S.C. 282, 422 S.E.2d 110 (1992). The test year provides a basis upon which a commission staff will conduct its audit of a company's books. Phillips, *The Regulation of Public Utilities* at 196. For rate-making purposes, only just and reasonable expenses are allowed; only used and useful property (with certain exceptions) is permitted in the rate base. *Id.* The commission must have a basis for estimating future revenue requirements. *Id.*

The Commission concludes that the appropriate test year to use in the instant proceeding is the twelve-month period ending December 31, 2000. No party contested the use of that test year as proposed by CWS in its Application. To the contrary, all parties relied upon that test year period in presenting their evidence.

3. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 3

According to CWS, due to its substantial plant investment, and specifically its rate base reflected on Schedule C of Exhibit "B" of its Application, the Company is entitled to have the reasonableness of its proposed rates determined in accordance with the rate of return on rate base methodology. Application, p. 4, ¶ 12. "The Public Service Commission has wide latitude to determine an appropriate rate-setting methodology." *Heater of Seabrook v. Public Serv. Comm'n of South Carolina*, 324 S.C. 56, 64, 478 S.E. 2d 826, 830 (1996). S. C. Code Ann. Section 58-5-240 (H) (Supp. 2000) directs the

Commission to specify an allowable operating margin in all water and wastewater orders. However, “that directive does not mean that the operating margin methodology must be used in determining a fair rate of return.” *Id.* Operating margin “is less appropriate for utilities that have large rate bases and need to earn a rate of return sufficient to obtain the necessary equity and debt capital that a larger utility needs for sound operation.” *Id.* According to the Application, CWS’s per books total rate base is \$12,188,532.⁵ None of the parties contested the Company’s request for rate base treatment. Due to the Company’s large rate base and its need to earn a fair and reasonable return on its investment, the Commission finds that return on rate base methodology is the appropriate rate-setting methodology to use in this case.

4. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4

The record reveals that the three rates of return witnesses, Ahern, Legler, and Spearman, used three components to determine the return on rate base. The three components are capital structure, cost of equity (or return on equity), and the cost of debt. “For regulatory purposes, the rate of return is the amount of money earned by a public utility, over and above operating costs, expressed as a percentage of the rate base. In other words, the rate of return includes interest on long-term debt, dividends on preferred stock and earnings on common stock (including surplus or retained earnings). Phillips. *The Regulation of Public Utilities* at 376. Additionally, “the return is that money earned from operations which is available for distribution among the various classes of contributors of money capital.” *Id.*

⁵ This amount does not reflect any adjustments to the rate base discussed herein.

5. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5

All three rate of return witnesses used the capital structure and cost of debt of Utilities, Inc., the parent company of CWS. Utilities, Inc. provided its cost of debt which was verified by the Commission's Audit Department. Use of the cost of debt for Utilities, Inc. is appropriate as the parent company provides all external financing for CWS and determines how much income CWS can retain. The capital structure for Utilities, Inc. at December 31, 2000, is 50.09% long-term debt and 49.91% equity, and the cost of debt of Utilities, Inc. at December 31, 2000, is 8.62%.

6. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6

Evidence concerning a fair return on equity (or cost of equity) was provided by witnesses Ahern, Spearman, and Legler. To determine the cost of equity, witnesses Ahern, Legler, and Spearman used the Discounted Cash Flow Model (DCF), the Capital Asset Pricing Model (CAPM) and the Risk Premium Model (RPM). Ahern and Legler also used the Comparable Earnings Model (CEM) to estimate the return on equity.

(1) Position of CWS:

CWS presented Pauline M. Ahern as its cost of capital witness. Witness Ahern is the Vice President of AUS Consultants- Utility Services. Ahern used the results from the application of the DCF approach, RPM, CAPM, and the CEM to determine a common equity cost rate. According to Ahern, no single cost of equity model is so inherently precise that it can be relied upon solely, to the exclusion of other theoretically sound models. Moreover, because all four models are based upon the Efficient Market Hypothesis (EMH) and have application problems associated with them, the EMH and

financial literature requires the assumption that investors rely upon multiple cost of common equity models.

Ahern assessed the market-based cost rates of similar risk companies, i.e. proxy groups, for insight into a recommended common equity cost rate for CWS. The proxy groups were used by Ahern because the Company's common stock is not publicly traded, and, therefore, CWS's market-based common equity cost rates cannot be determined directly. Therefore, Ahern used two proxy groups of water companies whose common stocks were actively traded for insight into an appropriate common equity cost rate applicable to CWS. The two proxy groups consist of eight and four water companies, respectively. To arrive at her common equity cost rate of 12.35%, Ahern reviewed the results of the application of four different costs of common equity models and then adjusted them upward to reflect CWS's greater risk compared to the proxy groups.

Ahern selected the proxy group of eight C.A. Turner water companies because they were included in the Water Company Group of C.A. Turner Public Utility Reports (June 2001) and they have Multex.com projected growth rates in earnings per share. Ahern Prefiled Direct Testimony, p.15. The four Value Line water companies were chosen because they are included in the Water Utility Group of Value Line Investment Survey (Standard Edition – May 4, 2001).

Ahern's results of the growth DCF cost rates for the proxy group of eight C.A. Turner Water companies is 9.2% and for the proxy group of four Value Line water companies is 9.8%. The results of the RPM analysis produced common equity cost rates of 13.1% for the eight C.A. Turner water companies and 13.0% for the proxy group of

four Value Line water companies. The CEM produces cost equity results of 12.8% for the proxy group of eight C.A. Turner water companies and for the proxy group of four Value Line water companies. Finally, the traditional CAPM cost rate is 11.5% for both the proxy group of eight C.A. Turner water companies and the four Value Line water companies. The empirical cost rate is 12.5% for both proxy groups. The CAPM cost rate applicable to both proxy groups is 12.0% based upon the traditional and empirical CAPM results. The average cost of equity for the proxy group of eight C.A. Turner water companies is 11.8% and the average for the proxy group of four Value Line water companies is 11.9%. Ahern then added an investment risk adjustment of .50% (50 basis points) to the average cost of equity of both proxy groups. Thereafter, the range of common equity rates, after adding the .50% investment risk adjustment, is 12.30% for the proxy group of eight C.A. Turner water companies and 12.40% for the proxy group of four Value Line water companies. Ahern then recommended a return on equity of 12.35%, which is the average of the common equity rates from her two proxy groups. In Ahern's opinion, the investment risk adjustment is necessary because CWS is a more risky investment than the average proxy group company due to CWS's small size compared to the two proxy groups, whether measured by book capitalization or the market capitalization of common equity. Ahern Direct Prefiled Testimony, p. 58. Ahern asserted that the loss of revenue from a few larger customers would have a greater effect on a small company than on a much larger company with a larger customer base. *Id.* at 11.

Using the capital structure of Utilities, Inc. consisting of 50.09% debt and 49.91% common equity, a cost of debt of 8.62%, and a cost of equity of 12.35%, Ahern concluded that an appropriate rate of return on rate base of 10.48% is applicable to CWS.

(2) Position of Staff:

Dr. James E. Spearman, Research and Planning Administrator for the Commission, presented Staff testimony regarding the cost of capital. To determine the estimate of the cost of equity, or return-on-equity, Dr. Spearman performed three separate analyses – the DCF, CAPM, and the RPM analyses. Because neither Utilities, Inc. nor CWS is publicly traded, Dr. Spearman applied the DCF and CAPM to a group of four water and wastewater companies reported in Value Line for comparison purposes.

Dr. Spearman's DCF analysis produced a return-on-equity range of 10.15% to 10.80%, and the CAPM analysis produced expected returns-on-equity in the range of 10.16% to 13.22%. The Risk Premium analysis produced expected returns-on-equity of 9.10% to 11.44%. The DCF and CAPM expected returns-on-equity overlapped between 10.16% and 10.80%. Overlap from the DCF and Risk Premium analyses occurred between 10.15% and 10.80%, while the CAPM and Risk Premium analyses overlap between 10.16% and 11.44%. Each methodology generated an expected return-on-equity of up to 10.80%, and the CAPM and Risk Premium methodologies produced an expected return-on-equity of up to 11.44%. Based on the consistencies of the methodologies, Dr. Spearman concluded that a return-on-equity for the water and wastewater industry would lie in the range of 10.00% to 11.50%.

However, Dr. Spearman acknowledged that determining the return-on-equity applicable to Utilities, Inc. and CWS is somewhat subjective. Dr. Spearman noted that Utilities, Inc. and CWS are much smaller than the water and wastewater companies of the comparison group. According to Dr. Spearman, smaller companies are considered to have more risk than larger companies. However, Dr. Spearman also stated his opinion that CWS would be viewed by an investor as having the risk of its parent, Utilities, Inc. It is also Dr. Spearman's opinion that Utilities, Inc., with most of its revenues derived from regulated operations, should have a risk similar to that of other regulated water and wastewater companies regardless of size. However, to account for size as a risk impact, Dr. Spearman considered the upper end of his narrowed range as an appropriate return-on-equity. Dr. Spearman opined that, based upon his analyses, a reasonable return-on-equity for CWS is 10.50% to 11.50%.

Using the capital structure of Utilities, Inc. consisting of 49.91% equity and 50.09% long-term debt, a cost of debt of 8.62%, and a cost of equity of 10.50% to 11.50% that Dr. Spearman found reasonable based upon his analyses, Dr. Spearman concluded that an appropriate return on rate base for CWS would lie in the range of 9.56% to 10.06%.

(3) Position of the Consumer Advocate:

Dr. John B. Legler testified as the cost of capital expert for the Consumer Advocate. Legler opined that the issue of the fair rate of return is still largely judgmental and that this is particularly true with respect to the issue of return on equity. Legler used CAPM, the bond yield plus risk premium method, and the DCF method. Legler also

provided the traditional comparable earnings method by analyzing rates of return on book equity earned by other companies with similar risks.

Dr. Legler applied the DCF model to a group of reasonably comparable water utilities followed by Value Line's Standard edition. Legler Direct Testimony at 13. Dr. Legler opined that when applying the DCF method to a single company, it is appropriate to use the average price of the Company's stock over a period of time rather than the price on a particular day. Moreover, Dr. Legler asserts that the use of a spot price in a situation where there are wide swings in the stock market over relatively short periods of time makes the resulting DCF calculation dependent upon the particular day chosen to perform the analysis—the use of the DCF method for ratemaking purposes must utilize a longer term view. Legler Direct Prefiled Testimony, p. 17. Dr. Legler uses three month average prices in his DCF analysis, and he also uses the closing prices on the last day of the three month period. The current time period in Legler's testimony is March through May 2001. *Id.* Dr. Legler's retention growth based on average prices produced results of 9.94% and on current prices 10.00%. Value Line dividend growth produced results of 6.67% based on average prices and 6.74% based on current prices. Value Line earnings growth produced results of 10.69% based on average prices and 10.76% based on current prices.

For his RPM analysis, Dr. Legler prepared a study for a group of water companies; this study was originally prepared for Dr. Legler's testimony in a case involving Southern California Water. Legler Direct Prefiled Testimony, p. 24. Dr.

Legler utilized the discounted cash flow approach to develop risk premiums. Dr. Legler's RPM analysis produced results of a range from 9.25% to 10.30%.

In Dr. Legler's CAPM analysis, he calculated the cost of equity for the group of reasonably comparable water utilities. For the entire sample of water utilities, the CAPM estimated return is in the range of 7.81% to 10.07%. For the companies covered in the Standard Value Line edition, CAPM produced results in a range of 8.37% to 10.64%. Finally for the companies covered in the Expanded Value Line edition, the CAPM produced results in a range from 6.67% to 9.43%.

Regarding his CEM analysis, Dr. Legler rejected the use of the comparable earnings approach using industrials as the only basis of comparison due to the questionable comparability of the measured earnings and differences in risks of regulated and unregulated companies. Dr. Legler provided the Value Line projected returns on book equity for the sample group of water companies. Dr. Legler opined that the projected returns provided little information on what reasonable allowed returns should be at the present time; however, in the interests of completeness, he provided them. For the Value Line sample of water companies, the projected returns average 10.13% for 2000, 10.50% for 2001 and 11.25% for 2002.

Using the capital structure of Utilities, Inc. consisting of 49.91% equity and 50.09% long-term debt, a cost of debt of 8.62%, and a cost of equity of 10.5%, Dr. Legler concluded an appropriate return on rate base for CWS would be 9.56%.

(4) Decision of the Commission:

Upon consideration of the appropriate cost of equity in this proceeding, we find that the appropriate return on equity to be 11.50%. This return on equity is on the upper end of Dr. Spearman's recommended range.

We reject witness Ahern's recommended cost of equity of 12.35%. We do not find it appropriate to add a separate risk premium to account for size.

We also reject Dr. Legler's recommended cost of equity of 10.50%. The record reveals that Dr. Legler utilized a study from a prior unrelated case involving Southern California Water as part of his RPM analysis. We find that his analysis in the instant case is flawed as he used a study for his RPM analysis which was unrelated to the instant proceeding. Dr. Legler also utilized the DCF, CAPM, and CEM methodologies to compute a recommended cost of equity. Similar to Dr. Spearman, Dr. Legler did not add a premium to his cost of equity to reflect the small size of CWS. Dr. Legler did state that small size is often associated with higher risk. However, we find no evidence that Dr. Legler considered size with his selection of 10.5%, which is the midpoint of his range. Thus, we reject Dr. Legler's recommendation as to the cost of equity.

We find Dr. Spearman's analysis the most convincing of the three opinions offered, and we are persuaded by Dr. Spearman's opinion that CWS, being a regulated utility, should have a risk similar to other regulated water and wastewater companies **regardless** of size. While we are of the belief that size is not as large a risk as witness Ahern opined, we consider the upper end of Dr. Spearman's range to account for size as a risk impact. Therefore, we find the appropriate return on equity for CWS to be 11.50%.

The Consumer Advocate asserted in cross-examination of CWS witness Ahern, and in his post-hearing brief, that the Company's Application sought a return on equity of only 10.7%. Thus, according to the Consumer Advocate, CWS has "admitted that 10.7% is a reasonable return on equity." Brief of Consumer Advocate at 7. Apparently, the Consumer Advocate asserts as a result that the Commission may not allow a return on equity in excess of that figure. The Consumer Advocate's analysis is flawed for several reasons.

First, contrary to the Consumer Advocate's assertion otherwise, the Company's application did not request that an "overall rate of return be set at 9.66%." Nowhere in its Application did the Company request a specific return on rate base. Rather, CWS only requested that it be allowed to charge the rates set forth in the rate schedule attached as Exhibit A to the Application. *See* Application, ¶ 4. In its prayer for relief, the Company asked only "...that the Commission approve the rates proposed and grant to Applicant such other and further relief as [we] may deem just and proper." Application at 4. Further, the Company is required to provide the Commission with a statement of its total plant investment with its application. 26 S.C. Code Ann. Regs. 103-512.4A.12 and 103-712.4.A.12. The inclusion of its rate base calculation with the Application satisfies this requirement. Likewise, the Company is required to provide the Commission with a pro-forma income and expense statement using proposed rates applied to the proposed test year. 26 S.C. Code Ann. Regs. 103-512.4.A.5 and 103-712.4.A.5. The Company also satisfied this requirement by submitting an income and expense statement which showed a proposed net operating income. The fact that the Company provided to the Commission

the return on rate base resulting from the proposed rate base and proposed net operating income cannot be reasonably construed as requesting a specific overall return any more than the omission of such a calculation could reasonably be construed as requesting no overall return.

Second, in the portion of the Application devoted to CWS's request for rate base treatment, CWS noted that its request for rate base treatment was based upon "its substantial plant investment, and specifically the rate base reflected on Schedule C of Exhibit "B". Application, ¶12. If we were to accept the Consumer Advocate's assertion that the Company can only be allowed a return on equity that is derived from the overall return resulting from the rates proposed in its Application, then we must also be constrained to use only the rate base which was specifically asserted in conjunction with that overall rate of return. And, it logically follows that we could only recognize the expenses asserted in the Company's Application which generate the revenue requirement for the overall return of 9.66%. We think that the folly of such an approach to ratemaking is self-evident.⁶

Moreover, in order to arrive at the 10.7% return on equity figure espoused by the Consumer Advocate, the Commission would have to do just as the Consumer Advocate suggests, and that is to "back out the return on equity" from the purportedly "requested"

⁶ Similarly flawed is the contention that the Company's response to Consumer Advocate Interrogatory No. 1-35 constitutes an admission that 10.7% is a reasonable return on equity. The interrogatory and response are directed at the Company's proposed water and sewer rate increases – not a proposed rate of return on equity or overall rate of return. And, again, the response is specifically based upon the Company's investment as set forth in the Application. The Commission cannot set rates in the piecemeal manner proposed by the Consumer Advocate, which is to impute to the Company a return on equity that can only be calculated using the rate base and expense figures proposed in the Application, yet ignore these figures for purposes of setting rates.

overall rate of return. To do so, the Commission would have to interpret the Application to request something that it plainly does not request.

Furthermore, the Consumer Advocate's analysis fails to recognize that for purposes of framing the issues in a rate case, the rates requested – not the calculated return which would result therefrom and set forth in an exhibit to the application – control. As the Supreme Court concluded in *Seabrook Island Property Owners Association v. South Carolina Public Service Commission et al.*, 303 S.C. 493, 401 S.E.2d 672 (1991), revisions to the financial and accounting exhibits provide no basis for a dismissal of an application as long as the rate schedules proposed by the utility are the same as initially filed with the Commission and noticed to the public. As in the *Seabrook* case, the Applicant in this case has never requested that the Commission approve rates other than those set forth in the proposed rate schedule. There is no question that the rates approved herein are less than those requested by the Company.

Finally, even if we were to accept the Consumer Advocate's contention and interpret the Application and interrogatory response as requesting an overall return of 9.66%, and thus a return on equity of 10.07%, the Consumer Advocate impliedly consented to a trial of the issue of whether the Company was entitled to a return on equity of 12.35% and an overall return of 10.48% as testified to by Company witness Ahern. See 26 S.C. Code Ann. Regs. R.103-870 (1976) and Rule 15(b), SCRCPP. The Consumer Advocate's own witnesses conceded that these figures were in issue. Specifically, in Hearing Exhibit No. 3, Consumer Advocate witness Bleiweis acknowledged that the Company's requested return on equity was 12.35% and overall return was 10.48%;

further, Mr. Bleiweis cited Consumer Advocate witness Legler as the source for these figures. Moreover, counsel for the Consumer Advocate never objected to the admission of witness Ahern's testimony on this point, choosing rather to cross-examine her in detail regarding the alleged disparity between her testimony and the content of the Application and interrogatory response. The issue of the appropriateness of a 12.35% return on equity was clearly tried and without objection by the Consumer Advocate. Accordingly, the Company's requests for a return on equity of 12.35% and overall return of 10.48% "...shall be treated in all respects as if they had been raised in the pleadings." *Sherman v. Sherman*, 307 S.C. 280, 282, 414 S.E.2d 809, 811 (Ct. App. 1992)

7. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 7

The return on rate base is determined by using long-term debt, equity, cost of debt and return on equity. When using the capital structure of Utilities, Inc. at December 31, 2000, of 50.09% long-term debt and 49.91% equity, a cost of debt of Utilities, Inc. at December 31, 2000, of 8.62%, and a return on equity of 11.50%, the appropriate rate of return on rate base for CWS is 10.06%. The following table indicates the capital structure of the Company, the cost of debt, the cost of equity as approved in this Order, and the resulting rate of return on rate base:

TABLE A

	RATIO	EMBEDDED COST	OVERALL COST
Long-term Debt	50.09%	8.62%	4.32%
Common Equity	<u>49.91%</u>	11.50%	<u>5.74%</u>
TOTAL	<u>100.00%</u>		<u>10.06%</u>

8. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 8

The evidence for the finding concerning the amount of the requested rate increase is contained in the Application filed by CWS and in the testimony and exhibits of Staff witness Richardson. The Application of CWS indicates that it is seeking additional revenues \$210,948 from water operations and additional revenues of \$474,115 from sewer operations, totaling \$685,063. Application of CWS, Schedule B, p. 1 of 4. Additionally, Staff witness Richardson testified that under the rates proposed in the Application CWS would see an increase in revenues of \$685,063. Richardson Prefiled Testimony, p. 2, ll. 12-14, Hearing Exhibit No. 7, p. 19. No party presented any evidence that the requested increase does not amount to \$685,063. Therefore, the Commission finds that CWS is seeking an increase in its revenues of \$685,063.

9. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 9

The Application of CWS shows per book test year total operating revenues of \$4,891,487. Application, Schedule B, p. 1 of 4. This amount includes “Uncollectibles” of \$28,220. Following the Staff audit of the Company’s books and records, Staff’s operating revenues agreed with the operating revenues stated by CWS in its Application. Staff calculated test year operating revenues of \$4,919,707. Hearing Exhibit 7, p. 19. Staff also included “Uncollectibles” of \$28,220 in the per books test year figures. Hearing Exhibit 6, Audit Exhibit AC. Thus, Staff computed per book test year total operating revenues of \$4,891,487. No other party presented any evidence to dispute either the Company’s or the Staff’s calculation of per book test year total operating revenues. Therefore, the only evidence before the Commission on per book total operating revenues is the \$4,891,487

as shown in the Company's Application and in the Staff's report in Hearing Exhibit No.

6. Therefore, the Commission finds that the appropriate per book test year total operating revenues are \$4,891,487.

10. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 10

The parties offered certain adjustments affecting operating expenses for the test year. CWS witness Wenz, Consumer Advocate witness Bleiweis, and Staff witness Scott offered testimony and exhibits detailing adjustments proposed by the parties. *See*, Hearing Exhibit 3 (Exhibits sponsored by Consumer Advocate witness Bleiweis), Hearing Exhibit 6 (Exhibits sponsored by Staff witness Scott), Hearing Exhibit 12 (Exhibits sponsored by CWS witness Wenz), and Hearing Exhibit 13 (Exhibit sponsored by CWS witness Wenz). This Section will address the adjustments offered which affect operating expenses.

(A) Operators' Salaries:

(1) Position of CWS: CWS proposed an adjustment to salaries of \$64,371. CWS annualized salaries using year-end payroll less per book wages.

(2) Position of Staff: Staff proposed to annualize the operators' salaries for the test year. Staff annualized the payroll at December 26, 2000, for total annualized wages of \$718,071. From this amount Staff subtracted per book wages of \$696,527 resulting in an adjustment for annualized wages of \$21,544. Staff then capitalized 20.87%, or \$4,496, of the wage adjustment and expensed \$17,048. Witness Scott testified that the wage capitalization rate used by Staff was based on the actual wages capitalized per books. Staff computed payroll taxes of \$1,575, of which \$329 was capitalized, and pension and

other benefits of \$1,373, of which \$287 was capitalized. Staff's total expense adjustment is \$18,134, consisting of wages of \$17,048 and pension and benefits of \$1,086.

(3) Position of Consumer Advocate: The Consumer Advocate did not oppose the Company's proposed adjustment for Operators' Salaries.

(4) Position of RHCA: RHCA proposed no adjustment for Operators' Salaries.

(5) Decision of the Commission: From the evidence presented at the hearing, the Commission is aware that the Staff adjustment included two parts: (1) to capitalize operators' salaries for the test year and (2) to remove 1 ½ operators' positions from the adjustment made by CWS. The Staff asserted that at the end of the test year there were 1 ½ vacant operators' position and thus the reason for the Staff proposing in its adjustment to remove those positions from CWS's proposed adjustment.

In rebuttal testimony, CWS witness Wenz submitted testimony that the ½ operator position should be allowed in this case. Witness Wenz stated that the operator splits his time between the Tega Cay service area and the CWS service area of River Hills. Wenz Prefiled Rebuttal Testimony, p. 3, ll. 7-8. Witness Wenz suggested that CWS allocates 2 ½ operators to the River Hills area and submits that such an allocation of manpower is reasonable.

Upon consideration of this adjustment, the Commission concludes that the operators' salaries should be capitalized to reflect the amount of time spent on capital projects during the test year. Staff appropriately determined the capitalization rate using actual wages capitalized per books. However, the Commission agrees with CWS that the ½ operator assigned to CWS's service area in River Hills should be allowed. The 2 ½

operators assigned by CWS to the River Hills service area is a reasonable allocation of manpower for that service area. Further, the use of one operator splitting time between the River Hills service area of CWS and the service area of Tega Cay (another company of Utilities, Inc.) is a resourceful allocation of personnel and assists the companies in keeping expenses at a minimum.

(B) Office Salaries:

(1) Position of CWS: The Company proposed an adjustment of \$15,216 to General & Administrative Expenses to annualize office salaries. CWS proposed a corresponding adjustment of \$8,550 to Taxes Other Than Income.

(2) Position of Staff: The Staff also proposed to annualize Office Salaries. Staff annualized the year-end payroll totaling \$94,950. From this amount, Staff subtracted the per book amount of \$98,164 for a net adjustment of (\$3,214). Staff also reduced payroll taxes by (\$246) and pension and benefits by (\$735). To account for its proposed wage adjustment to annualize Office Salaries, Staff adjusted General and Administrative Expenses by (\$3,214) and pension and benefits by (\$735), for a total adjustment of (\$3,949).

(3) Position of Consumer Advocate: The Consumer Advocate did not disagree with the Company's proposed adjustment to Office Salaries.

(4) Position of RHCA: RHCA did not propose an adjustment for Office Salaries.

(5) Decision of the Commission: The evidence from Staff witness Scott reveals that the Staff adjustment removes one terminated employee from the annualized year end

salaries. Scott Prefiled Testimony, p. 5, ll. 16-17, Hearing Exhibit No. 6, Audit Exhibit A-1, p. 1 of 15. CWS included the terminated employee in its adjustment.

There was no evidence presented that the terminated employee has been replaced. Nor has any evidence been presented that the employee will be replaced or that his services are necessary. Therefore, the Commission adopts the adjustment proposed by the Staff as the Staff's adjustment reflects the actual test year and there is nothing in the record to warrant an out-of-test year adjustment.

(C) Employee Bonuses:

(1) Position of CWS: CWS did not propose an adjustment to this item.

(2) Position of Staff: Staff proposed to remove holiday bonuses for CWS and WSC employees as Staff considers bonuses to be the responsibility of the stockholders, not the ratepayers. Full-time employees received a bonus of \$100 and part-time employees received \$50. Staff removed \$2,381 for bonuses for CWS employees and WSC⁷ bonuses allocated to CWS of \$136, which included FICA expense.

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment on this item.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: The Commission finds that the Staff adjustment with regard to removal of employee holiday bonuses from test year expenses should be adopted. CWS witness Wenz testified on cross examination during his rebuttal testimony that bonuses are not always awarded and are determined by the Board of

⁷ WSC is Water Service Corporation, which is a sister company of Carolina Water Service. WSC performs the tasks of allocating common expenses among the Utilities, Inc. subsidiaries.

Directors. The Commission agrees with the Staff reasoning that employee bonuses should be the responsibility of the shareholders and not the ratepayers. As such, the employee bonuses should be removed from test year expenses.

(D) Update Customer Equivalents:

(1) Position of CWS: CWS did not propose an adjustment to Update Customer Equivalents.

(2) Position of Staff: The Staff proposes to adjust common expenses, direct salaries, Charlotte warehouse, Charlotte office, and the Columbia office for customer equivalents updated to December 31, 2000. Staff recalculated the allocation factors and applied the factors where applicable in the allocation process. Staff's recalculation decreased Operating and Maintenance expenses by (\$10,665), General and Administrative expenses by (\$753), Depreciation and Amortization by (\$351), and Taxes Other Than Income by (\$845).

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment on this item.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: The Staff's adjustment results from recalculating allocation factors to the end of the test year of December 31, 2000. Staff witness Scott presented evidence that the allocations of CWS were based on customer equivalents at June 30, 2000. Hearing Exhibit 6, Audit Exhibit A-1, p. 2 of 15. The Commission finds it appropriate to adopt the Staff adjustment which uses allocation

factors from the end of the test year. Use of the end of the test year allocations matches with other adjustments annualized at the end of the test year.

(E) Rate Case Expenses:

(1) Position of CWS: CWS updated its rate case expenses at the hearing on August 6, 2001, and seeks recovery of rate case expenses of \$132,964. CWS's adjustment consists of expenses incurred as of the August 6, 2001 hearing of \$117,298 plus estimated post-hearing expenses of \$15,666. CWS proposed to amortize rate case expenses over a three year period.

(2) Position of Staff: In its prefiled testimony and exhibits, the Staff included an adjustment for rate case expenses of \$42,087, representing the amount of rate case expenses that the Staff verified in its audit of the Company's books and records. Staff proposed to amortize the rate case expenses over a three year period, resulting in an adjustment of \$14,029. At the hearing on August 6, 2001, the Company updated its rate case expenses as of the date of the hearing. The Company provided invoices for legal fees and an expert witness, as well as documentation of travel expenses associated with witnesses' travel to the hearing on July 11, 2001, and August 6, 2001. The Company's updated rate case expenses totaled \$117,298. Staff accepted, subject to check, this amount as the expenses incurred in relation to the instant rate case. By its Post-Hearing Brief, the Staff recommended adoption of rate case expenses of \$116,793.⁸ Staff proposes to amortize this amount over a three year period which would result in a total adjustment of \$38,931.

⁸ The difference in the rate case expenses proposed by the Company and the rate case expenses proposed by the Staff amounts to \$505 and results from a difference in the amount allowed for CWS personnel in preparing and working on the rate case.

(3) Position of Consumer Advocate: The Consumer Advocate recommended that the Commission allow total rate case expense of no more than \$120,000, with \$100,000 for legal fees, travel, and WSC personnel, and \$20,000 for the cost of capital witness. The Consumer Advocate proposed a five year amortization period for this expense.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: As testified to by Staff witness Scott, there must be a “cut-off” of the time within which CWS may seek adjustments for rate case expenses. The proposition is certainly a correct statement. The question of when that “cut-off” should be established is at the heart of this adjustment.

Staff’s audit was conducted months before this case reached the posture of hearing. Thus, it must be recognized that many expenses associated with the case were not yet incurred. CWS has provided evidence in the form of invoices as to expenses as of the August 6, 2001, hearing showing a total of \$117,298 in unaudited rate case expenses. This amount reflects expenses associated with WSC personnel in the preparation of the rate case, cost of an expert witness related to the cost of capital issue, travel expenses, and legal expenses. In addition to the amount for which CWS has provided invoices, CWS seeks additional expenses of \$15,666 which represent an “estimate” of costs for “post-hearing” work related to the case.

The Consumer Advocate’s witness proposed that the Company should be granted no more than \$120,000 in rate case expenses. The Consumer Advocate witness also referenced the expenses associated with the last rate case in making his recommendation. This comparison lends little to the discussion before this Commission. In the instant case,

the Company and its counsel have attended three night hearings, and the hearing before the Commission has required two days. Further, this case involves the use of cost of capital witnesses. The Commission does not find it appropriate to compare the expenses from the prior rate case as a benchmark upon which to determine the appropriate expenses associated with the instant case.

As CWS has provided documentation in the form of invoices and billings as of the date of the August 6, 2001, hearing, the Commission finds that the August 6, 2001, hearing is the appropriate “cut-off” for rate case expenses. CWS has demonstrated rate case expenses of \$116,793, as verified and corrected by Staff, as of August 6, 2001. The Commission finds that it would not be appropriate to establish a “cut-off” as of the Staff audit as the Commission recognizes that the Staff audit occurs early in the rate case proceeding. Further, in the instance of this case, the Commission does not find it appropriate to establish the “cut-off” as of the July 11, 2001, hearing date as through unavoidable circumstances the hearing could not have been completed on that date. The Commission does however find that the August 6, 2001, hearing date is an appropriate “cut-off” for rate case expenses in the instant case.

The adjustment of \$116,793 as corrected by Staff is a known and measurable expense that the Commission may properly consider in establishing rates. The Commission is guided in its decision by the case of *Heater of Seabrook, Inc. v. Public Service Commission of South Carolina*, 324 S.C. 56, 478 S.E.2d 826 (1996), in which the Supreme Court of South Carolina stated “[w]hen calculating expenses in rate cases, Commission should use only test year data and known and measurable changes occurring

after the test year.” In the instant case, the amount of rate case expenses approved herein are known and measurable as they are supported by invoices and billings. Further, as rate case expenses are expenses that occur in the preparation of and defending a rate case, they are by their very nature occurring after a test year. Thus, the rate case expenses at issue in the instant proceeding meet the known and measurable standard for out-of-test year occurrences as stated in the *Heater* case, *supra.*, and the Commission finds it appropriate to allow an adjustment for rate case expenses in this proceeding.

The next step is for the Commission to consider how the rate case expenses should be recovered. CWS and the Staff both propose amortization periods of three years. The Consumer Advocate proposes an amortization period of five years. Ideally, the amortization period should be for the period between rate cases. However, it is impossible to foresee what the future holds and to state with any certainty when the Company may need to return to this Commission for rate adjustment. The last rate case for CWS was in 1994, or seven years ago. *See*, Hearing Exhibit 6, p.2. Prior to that case, CWS had rate cases in 1993, 1990, 1989, and 1986. *Id.* Thus the difficulty of setting an appropriate amortization period is certainly apparent. None of the amortization periods proposed by the parties match precisely with the frequency with which the Company has had rate cases. While the Company’s last rate case was seven years ago, the dates of the cases from 1986 through 1994 show that cases were filed three years apart, then one year, then three years, then one year.

In *Hamm v. South Carolina Public Service Commission*, 309 S.C. 282, 422 S.E.2d 110 (1992), the Supreme Court of South Carolina stated

Adjustments for known and measurable changes in expenses may be necessary in order that the resulting rates reflect the actual rate base, net operating income, and cost of capital. The adjustments are within the discretion of the Commission and must be known and measurable within a degree of reasonable certainty. Absolute precision, however, is not required.

(citing *Michaelson v. New England Tel. & Tel. Co.*, 121 R.I. 722, 404 A.2d 799 (1979)).

While the Commission cannot state with absolute precision when the Company will return for another rate proceeding, the Commission must provide a sufficient amortization period under which CWS may recover its expenses. After reviewing the frequency of the Company's previous rate cases, the Commission finds that an amortization period of three years is an appropriate time to recover the rate case expenses approved herein. The record supports a three year amortization period as reflected in the testimonies of Witness Wenz and Witness Scott.

Therefore, the Commission approves rate case expenses of \$116,793 and sets a three-year amortization period for the recovery of those expenses. The result is an adjustment to the test year of \$38,931 for rate case expenses related to instant case.

(F) Deferred Expenses:

(1) Position of CWS: CWS did not propose an adjustment to this item.

(2) Position of Staff: Staff proposed an adjustment of (\$20,316) for Deferred Charges. Expenses Staff removed from Deferred Expenses were recurring, anticipated expenses such as tank maintenance for water operations, pressure washing and jetting sewer mains, TV camera for sewer mains, and regulatory expenses which were not related to CWS.

(3) Position of Consumer Advocate: The Consumer Advocate recommends an adjustment of (\$76,706) to remove all items from Deferred Legal Expense and Deferred Maintenance Expense.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: In *Porter v. South Carolina Public Service Commission*, 328 S.C. 222, 493 S.E.2d 92 (1997), the Supreme Court of South Carolina stated that “[t]he expenses described by witness ... are routine and required at regular intervals. They therefore do not qualify as extraordinary because they are not unanticipated or non-recurring.”

Staff witness Scott stated in her testimony that the Commission Staff removed anticipated and recurring items from per book amount Deferred Expenses of \$76,706, for a net reduction to the per book numbers of (\$20,316). Scott Prefiled testimony, p. 7, ll. 12-14. Expenses removed by the Staff included recurring expenses such as tank maintenance for water operations, pressure washing and jetting sewer mains, TV camera for sewer mains, and regulatory expenses which were not related to CWS. *Id.* at ll. 4-6. Further witness Scott explained that Attorney Fees for Lake Murray Bulk Water Agreements of \$2,087, the I&I study of \$8,674, and expenses associated with various regulatory matters which include the Erwin Complaint, Bulk Rate issues, Rate Case Appeal of 1998, and issues with the Landings and Clover School District, totaling \$271,187 were included in Deferred Charges. *Id.* at ll. 6-11. Staff amortized these expenses, totaling \$281,948, over five years for a total adjustment of \$56,390. Staff

subtracted the per book amount for Deferred Expenses of \$76,706, for a net reduction to the per book numbers of (\$20,316).

Consumer Advocate witness Bleiweis recommended removing all expenses which CWS booked as Deferred Expenses. Witness Bleiweis recommended removing Deferred “Legal” Expenses of \$61,590 and Deferred “Maintenance” Expenses of \$15,116 for a total adjustment of \$76,706. Bleiweis Prefiled Testimony, p. 10.

The Commission adopts the adjustment proposed by the Staff. Based upon *Porter v. South Carolina Public Service Commission, supra*, the Staff correctly removed items from Deferred Expenses that are not extraordinary but are in fact routine and recurring.

(G) Non-allowable Expenses:

(1) Position of CWS: CWS did not propose an adjustment for Non-allowable Expenses.

(2) Position of Staff: Staff proposed a total adjustment of (\$20,320) to disallow expenses which Staff considers non-allowable for ratemaking purposes.

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment for Non-allowable Expenses.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: Upon consideration of this adjustment, the Commission adopts the adjustment proposed by the Staff. Staff witness Scott testified that Staff disallowed direct expenses to CWS which included flowers, a billing error, 1/2 Chamber of Commerce dues, and items for which CWS does not provide support for total non-allowable direct expenses amounting to \$19,479. Scott Prefiled testimony, p. 7, ll.

16-21; Hearing Exhibit 6, Audit Exhibit A-1, p. 4 of 15. Staff also disallowed WSC common expenses allocated to CWS, which Staff considers non-allowable for ratemaking purpose, including expenses for out of test year expenses, flowers, 1/2 Chamber of Commerce dues, and employee newsletters. Staff also reclassified items which should be capitalized. A total of \$12,323 of WSC common expenses were non-allowable, of which CWS was allocated \$841 or 6.823%. Scott Prefiled testimony, p. 7, l. 21 – p. 8, l. 4; Hearing Exhibit 6, Audit Exhibit A-1, p. 4 of 15.

The Commission agrees with the Staff's removal of these expenses discussed in the preceding paragraph. Not all expenditures by a utility will be allowed in a proceeding to establish rates. The expenses discussed are not expenses which provide a direct benefit to the ratepayers. Therefore, the Commission agrees that the expenses should be removed from test year expenses.

(H) Depreciation Expense Adjustment:

(1) Position of CWS: CWS proposed an adjustment of \$26,917 to annualize Depreciation Expense.

(2) Position of Staff: Staff proposed to annualize Depreciation Expense with an adjustment of (\$32,970). The Staff's adjustment included completed plant of \$23,239 added to Gross Plant of \$31,616,926. Gross Plant was then reduced by Organization Expense, Land, Vehicles, Computers, CIAC, Plant Acquisition Adjustment, and Advances in Aid, for Net Plant of \$15,480,429. Staff then applied the depreciation rate of 1.50% to the net amount of \$15,480,429. Staff then depreciated vehicles not fully depreciated and computers at 20%. Moreover, Staff computed the WSC Rate Base

depreciation expense and decreased Depreciation Expense for annualized excess book value. Staff's total computed Depreciation amounted to \$254,952 less the per book amount of \$287,922 results in a net adjustment of (\$32,970). Depreciation rates used by the Staff were recommended by the Utilities Department.

(3) Position of Consumer Advocate: The Consumer Advocate agreed with the Depreciation Adjustment proposed by the Company less a reduction of (\$4,334) in Depreciation Expense to reflect the Consumer Advocate's recommended reduction in Pro Forma Plant.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: Upon consideration of this adjustment, the Commission finds the adjustment proposed by Staff to be appropriate. According to Staff witness Scott, the adjustment proposed by CWS (a) included plant additions estimated at \$372,950, (b) did not reduce gross plant for organizational expenses and computers before applying 1.5% for depreciation expense, and (c) did not remove fully depreciated vehicles, did not include WSC Rate Base Depreciation Expense, and did not reduce depreciation by the amortization of Excess Book Value. Scott Prefiled testimony, p. 8, l. 20 – p. 9, l. 3.

The Commission rejects the adjustment proposed by CWS because estimated plant additions are not appropriate for inclusion in depreciation expense and fully depreciated items must be removed from the expense account. Thus the adjustment proposed by CWS is flawed and must be rejected. Staff's adjustment, however, included

only completed plant, removed fully depreciated items, and removed other items properly removed from the account.

(I) Lease to Bio Tech:

(1) Position of CWS: CWS did not propose an adjustment for this item.

(2) Position of Staff: The Staff proposed an adjustment of (\$3,744) to remove Depreciation Expense associated with Bio Tech, a sister company of CWS, which shares the West Columbia office building.

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment for this item.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: The Commission finds the Staff adjustment appropriate and adopts the Staff's adjustment. Staff witness Scott testified that Staff reviewed the lease agreement and found that Bio Tech leases 4,400 square feet (51%) of the 8,600 square foot building owned by CWS. Scott Prefiled testimony, p. 9, ll. 7-10. The term of the lease is five years, beginning July 18, 1997, and the entire amount of the rent is for a sum of \$5.00. *Id.* Staff proposes to allocate 51% of the depreciation expense to Bio Tech. *Id.* at ll. 10-11. Staff did not remove any other operating expenses since Bio Tech is responsible for paying its own expenses such as 1/2 real estate taxes, utilities, security system, and repairs and maintenance. *Id.* at ll. 11-13. Staff verified total gross plant of \$487,768 and applied the depreciation rate of 1.50%, amounting to \$7,317. Staff allocated 51%, or (\$3,744), to Bio Tech and removed (\$3,744) from Depreciation Expense. *Id.* at ll. 13-15.

The Commission finds the staff adjustment reasonable and appropriate. As CWS does not utilize the entire building and as the ratepayers of CWS do not receive a benefit from the entire building, it is appropriate to remove from the expenses of CWS that portion of the building which CWS does not use.

(J) Expenses Associated with River Hills, I-20, and Watergate:

(1) Position of CWS: CWS agreed that the taxes paid in Lexington County should be removed from test year expenses. However, the Company did not agree with Staff's adjustment as it relates to removing expenses associated with River Hills.

(2) Position of Staff: The Staff proposed an adjustment of (\$7,736) to remove property taxes associated with plant in the River Hills subdivision and the I-20 and Watergate service areas that Staff considers to no longer meet the "used and useful" standard. Staff also computed depreciation expense associated with these unused wells in the River Hills subdivision, I-20 service area, and Watergate service area by applying the depreciation rate of 1.50% to the depreciable plant. The total depreciable plant for River Hills, I-20, and Watergate amounted to \$493,406, resulting in a proposed adjustment of (\$7,401) for depreciation expense.

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment for this item.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission:

CWS has bulk water agreements with York County, the City of West Columbia, and Lexington County Joint Water and Sewer Commission to provide water to the River

Hills subdivision, the I-20 service area, and the Watergate service area, respectively. Based upon the bulk water supply agreements that allow an entity other than CWS to supply the water, Staff concluded that the wells and other plant items no longer meet the “used and useful” standard as those wells and plant items are not used in providing water to the CWS customers. *See*, Scott Prefiled Testimony, p. 9, l.18 - p. 10, l.1. Thus Staff proposed that the expenses associated with the wells and other plant items be removed from operating expenses. According to Staff witness Scott, CWS has provided information that the only test year expenses associated with those wells are property taxes. *Id.* at 10, ll. 2-6. Staff calculated an adjustment of (\$7,736) for property taxes. Staff also calculated an adjustment to Depreciation Expense of (\$7,401).

CWS witness Wenz testified in rebuttal that CWS agreed with the Staff’s proposed adjustments for the water wells in the I-20, Lexington, and Watergate systems. He further admitted that those plants are no longer used and useful in the provision of service to the customers. According to Company witness Wenz, the Company has not taken the River Hills wells off-line but is maintaining those wells in back-up status. Mr. Wenz also stated that no expenses other than taxes have been included in test year expenses for operation and maintenance of the River Hills wells as the wells have not been operated since the interconnection with York County in 1996.

Upon consideration of this item, the Commission finds that the adjustments proposed by the Staff should be adopted. The Company admits that the wells in the I-20 and Watergate areas are no longer used and useful and that the expenses associated with those wells should be removed from test year expenses. However, the Commission finds

that the Company's assertion that the wells in the River Hills service area are providing a "benefit" to customers does not rise to the level of "used and useful" for inclusion of those expenses in the test year. CWS admits that the wells in the River Hills service area were not used to provide water to customers during the test year. As such, those wells do not meet the definition of property used and useful in providing service to customers, and therefore, the expenses associated with those wells are properly deducted from test year expenses.

Further, the Commission finds that the expenses associated with the Idlewood and Westside Terrace service area should also be removed. While Staff did not include an adjustment to remove the Idlewood and Westside Terrace expenses, Staff noted in its testimony that the Idlewood and Westside Terrace had requested approval of bulk water agreements. Prefiled Testimony of Scott, p. 16, ll. 3-6. Staff calculated test year expenses associated with the wells of these systems of \$990, comprised of \$823 for property taxes and \$167 of depreciation expense. *Id.* at ll. 18-20. As will be seen in the discussion on rate base, the Commission in this Order is removing the wells of Idlewood and Westside Terrace from rate base. Therefore, the Commission finds it appropriate to also remove the test year expenses associated with that plant. The Commission therefore adopts an adjustment of (\$990) to remove the expenses of the Idlewood and Westside Terrace subdivisions from the test year.

(K) Gross Receipts Tax Increase:

(1) Position of CWS: CWS proposed an adjustment of \$2,850 for an estimated 5% increase in Utility Commission Taxes.

(2) Position of Staff: Staff did not allow for a separate adjustment for Gross Receipts Tax Increase as Staff was unable to verify the Company's increase. Staff used the most current gross receipts factor in the adjustment for the proposed increase.

(3) Position of Consumer Advocate: The Consumer Advocate removed the adjustment proposed by CWS. The Consumer Advocate witness stated that the adjustment does not meet the “known and measurable” standard.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: Upon consideration of this item, the Commission adopts the position advanced by the Consumer Advocate and Staff. There is nothing in the record to support a 5% increase in Utility Commission Taxes (or Gross Receipts Tax.) Witness Bleiweis was correct in his assessment that an “estimated” increase to a tax does not meet the “known and measurable” standard. Therefore, the Commission rejects this proposed adjustment by CWS.

(L) Income Taxes:

(1) Position of CWS: CWS proposed an adjustment of \$440 to adjust taxes for accounting and pro forma adjustments. CWS used a 5% rate for state taxes and a 34% rate for federal taxes.

(2) Position of Staff: The Staff also proposed to adjust for the effect of income taxes after accounting and pro forma adjustments. Like CWS, the Staff used a 5% rate for state taxes and a 34% rate for federal taxes.

(3) Position of Consumer Advocate: The Consumer Advocate likewise adjusted Income Taxes for the tax effect of accounting and pro forma adjustments.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: The Commission adopts the method proposed by the Staff and the Company to adjust taxes for accounting and pro forma adjustments. The Commission finds that a 5% rate for state taxes and a 34% rate for federal taxes is appropriate as those are the actual tax rates that apply to CWS. The methodology is adopted for use in this proceeding, but the actual adjustments will vary from the proposed adjustments as the adjustments adopted herein are different than the adjustments used by the parties in their calculations. Based on the adjustments adopted herein, the Commission approves an adjustment for Income Taxes of \$80,830 for the tax effect of accounting and pro forma adjustments.

(M) Customer Deposits:

(1) Position of CWS: The Company did not propose an adjustment for this item.

(2) Position of Staff: The Staff proposed an adjustment to annualize Interest on Customer Deposits by using the account balance as of December 31, 2000, of \$159,022 and by applying the Commission approved interest rate of 8%. Staff computed annualized Interest on Customer Deposits of \$12,722 less the per book amount of \$12,910 for an adjustment of (\$188).

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment for this item.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: The Commission adopts the adjustment proposed by the Staff. This adjustment annualizes the Interest on Customer Deposits at

the end of the test year at the interest rate of 8%, which is the Commission approved rate for interest on customer deposits.

(N) Allowance for Funds Used During Construction (AFUDC):

(1) Position of CWS: CWS proposed an adjustment of (\$17,478) to remove the Allowance for Funds Used During Construction (“AFUDC”).

(2) Position of Staff: The Staff proposed to remove only the AFUDC associated with plant items which have been closed to plant in service and proposed to remove (\$3,147) from AFUDC.

(3) Position of Consumer Advocate: The Consumer Advocate did not object to the Company’s proposed adjustment to AFUDC.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: AFUDC is allowed as an offset to the interest capitalized when plant is under construction. Scott Prefiled Testimony, p. 11, ll. 18-19. While both the Staff and CWS propose to remove income associated with capitalized interest on projects under construction, CWS proposes to remove the total AFUDC while Staff proposes to remove only the AFUDC associated with plant items which have been closed to plant in service. *Id.* at ll. 16-21. Staff witness Scott testified that Staff verified the AFUDC associated with the closed projects and proposes to remove that portion from AFUDC. *Id.* at p. 11, l. 21 – p. 12, l. 2.

The Commission adopts the Staff’s adjustment on this item. As AFUDC is allowed as an offset to the interest capitalized when plant is under construction, it is only appropriate to remove from AFUDC that portion which is associated with projects that

have in fact been closed to plant in service. There is no support to remove the entire amount from AFUDC as proposed by CWS.

(O) Expense Variance:

(1) Position of CWS: CWS did not propose an adjustment for this item on the premise that the Consumer Advocate's adjustment does not reflect known and measurable changes to test year expenses.

(2) Position of Staff: The Staff did not propose an adjustment for this item.

(3) Position of Consumer Advocate: The Consumer Advocate proposed an adjustment of (\$64,519) to Operation and Maintenance ("O&M") Expenses to reflect abnormal expenditures.

(4) Position of RHCA: RHCA did not propose an adjustment on this item.

(5) Decision of the Commission: Consumer Advocate witness Bleiweis proposed an adjustment to Transmission and Distribution Materials and Supplies (Sewer) expense on the basis that the test year expense was abnormal when compared with the expense of that account from the previous two calendar years. Bleiweis Prefiled Direct Testimony, p. 13, 11-19. Witness Bleiweis proposes that the Commission adopt the three year average of expenses in that account which results in an adjustment of (\$64,519) to O&M expense. *Id.* at p. 14, 11.7-8.

CWS witness Wenz testified that simply taking a three year average of this expense category violates the known and measurable standard. Wenz Rebuttal Testimony, p. 9, 11. 11-13. Witness Wenz further opined that the witness for the

Consumer Advocate offered no evidence that the expenses were imprudently incurred or that expenses would decrease over time. *Id.* at ll. 13-14.

In *Hamm v. South Carolina Public Service Commission*, 309 S.C. 282, 422 S.E.2d 110 (1992), the Supreme Court of South Carolina stated “[a]lthough the burden of proof of the reasonableness of all costs incurred which enter into a rate increase request rests with the utility, the utility’s expenses are presumed to be reasonable and incurred in good faith.” The Supreme Court further stated that “[w]here an unusual situation exist which shows that the test year figures are atypical and thus do not indicate future trends, the Commission should adjust the test year data.” *Id.* at 289-90.

Upon consideration of this adjustment, the Commission concludes that the adjustment does not indicate an unusual situation which would require an adjustment to the test year data. In fact, the data presented by the witness for the Consumer Advocate indicates that the expenses in that account have risen each of the three years cited. There is nothing in the record to suggest that any of the expenses from the test year were imprudently incurred nor, as suggested by CWS witness Wenz, is there any evidence of record to suggest that the expenses would decrease. The Commission therefore rejects the adjustment for expense variance proposed by the Consumer Advocate.

Summary of Adopted Adjustments to Expenses:

The total effect of the adjustments to test year expenses adopted herein increase Operating and Maintenance Expenses by \$3,598, increase General and Administrative Expenses by \$22,381, reduce Depreciation and Amortization Expenses by (\$14,376), reduce Taxes Other Than Income by (\$13,122), increase Income Taxes by \$80,830,

reduce Interest on Customer Deposits by (\$188), and reduce AFUDC by (\$3,147). The net effect of the adjustments adopted herein on Total Operating Expenses is to increase Total Operating Expenses by \$79,122. Thus, operating expenses for the test year under present rates and after accounting and pro forma adjustments and adjustments for known and measurable out-of-test year occurrences are \$4,012,749.

The following table indicates the Company's gross revenues for the test year after adjustments approved herein, under the presently approved rate schedules; the Company's operating expenses for the test year after accounting and pro forma adjustments and adjustments for known and measurable out-of-test year occurrences approved herein; and the rate of return on rate base under the presently approved schedules for the test year:

TABLE B

	<u>Before Increase</u>
Operating Revenues	\$4,891,487
Operating Expenses	<u>4,012,749</u>
	\$ 878,738
ADD: Allowance for Funds Used During Construction	14,601
Customer Growth	<u>7,477</u>
TOTAL INCOME FOR RETURN	<u>\$ 900,816</u>
Return on Rate Base	<u>7.86%</u>

11. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 11

The parties offered certain adjustments affecting the Company's rate base for the test year. CWS Witness Wenz, Consumer Advocate witness Bleiweis, and Staff witness Scott offered testimony and exhibits detailing adjustments proposed by the parties. See,

Hearing Exhibit 3 (Exhibits sponsored by Consumer Advocate witness Bleiweis), Hearing Exhibit 6 (Exhibits sponsored by Staff witness Scott), Hearing Exhibit 12 (Exhibits sponsored by CWS witness Wenz), and Hearing Exhibit 13 (Exhibit sponsored by CWS witness Wenz). This Section will address the adjustments offered which affect the Company's rate base.

(A) Capitalized Wages and Benefits:

(1) Position of CWS: CWS did not propose an adjustment for this item.

(2) Position of Staff: Staff proposed an adjustment to capitalize wages associated with the annualization of the operators' salaries. Staff's adjustment capitalizes 20.87% of the test year wages and benefits which amounts to \$5,112. Staff witness Scott testified that Staff's capitalization rate was based on the actual wages capitalized during the test year.

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment for this item.

(4) Position of RHCA: RHCA did not propose an adjustment for this item.

(5) Decision of the Commission: The Commission finds Staff's adjustment appropriate and hereby adopts the adjustment. This adjustment corresponds with a portion of the adjustment the Commission adopted under Expenses. Therefore, the Commission adopts Staff's adjustment of \$5,112.

(B) Officers' Bonuses and Salary Increases:

(1) Position of CWS: CWS asserts that Staff has only looked at one side of the equation and asserts that the Staff adjustment to lower officer group's capitalized time rates should result in additional expense allocated to the Company.

(2) Position of Staff: The Staff proposes to remove bonuses and officers' salary increases from capitalized wages. Staff recomputed capitalized salary rates to include only the base salary, payroll taxes, pension and benefits. Staff computed total capitalized salaries of \$51,562 less per book salaries of \$95,458 for a total adjustment of (\$43,896). Staff also proposes to disallow officers' test year salary increase of 3% for an adjustment of (\$1,502).

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment for this item.

(4) Position of RHCA: RHCA did not propose an adjustment for this item.

(5) Decision of the Commission: The Commission agrees with the Staff adjustment as proposed. CWS witness Wenz testified at the hearing that bonuses are not always offered and that bonuses are awarded by the Board of Directors. It is the Staff's position that bonuses should be the responsibility of the shareholders and not the ratepayers. The Commission agrees that Staff's position is reasonable and appropriate.

(C) Plant Sample Items – CWS:

(1) Position of CWS: CWS did not propose an adjustment for this item.

(2) Position of Staff: Staff proposed to disallow test year plant additions of (\$8,661) for which the Company was unable to provide support. Staff also reclassified (\$192) for items which should be expensed.

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment for this item.

(4) Position of RHCA: RHCA did not propose an adjustment for this item.

(5) Decision of the Commission: The Commission adopts the adjustment proposed by Staff. As CWS could not provide support for the plant additions disallowed by Staff in its adjustment, the Commission finds that those items should not be included in the rate base. Without support for the items, there is no way to determine whether the items are properly included in the rate base.

(D) Plant Sample Items – WSC:

(1) Position of CWS: CWS did not propose an adjustment for this item.

(2) Position of Staff: The Staff proposed to allocate a portion of expenses which should have been capitalized. Staff removed \$3,587 from WSC's expenses for a mailing machine and allocated 7.10% of the mailing machine to CWS, amounting to \$255. The Staff allocated the WSC expense using the WSC rate base allocation composite factor of 7.10%.

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment for this item.

(4) Position of RHCA: RHCA did not propose an adjustment for this item.

(5) Decision of the Commission: The Commission adopts the adjustment proposed by Staff. Staff's adjustment capitalizes a mailing machine that had been expensed. The Commission agrees with the Staff that a mailing machine is a capital item rather than an expense item.

(E) Plant Additions:

(1) Position of CWS: CWS proposed an adjustment of \$372,950

(2) Position of Staff: Staff proposed an adjustment to Plant in Service of \$23,239 and an adjustment of (\$13,326) to Construction Work in Progress (“CWIP”). Of the \$23,239 total adjustment, \$9,913 is a plant addition and \$13,326 is transferred from CWIP.

(3) Position of Consumer Advocate: The Consumer Advocate proposed an adjustment of (\$288,950) to Pro Forma Plant and an adjustment of (\$182,910) to CWIP.

(4) Position of RHCA: RHCA did not propose an adjustment for this item.

(5) Decision of the Commission: CWS proposed an adjustment to Pro Forma Plant of \$372,950. Application, Exhibit B, p. 6 of 13. The stated reason in the Application for the adjustment was “Pro Forma Plant is adjusted for planned capital investments.” Application, Exhibit B, p. 7 of 13. Witness Wenz testified that this adjustment was to reflect capital projects that were underway but not yet complete as of the end of the test year. Wenz Direct Prefiled Testimony, p. 7, ll.11-13. Wenz further stated that the Pro Forma Plant is needed to provide end of test year customers with safe and reliable water and sewer service. *Id.* at ll. 13-14.

Consumer Advocate witness Bleiweis proposed to adjust Pro Forma Plant by (\$288,950) and to reduce CWIP by (\$182,910). Bleiweis Direct Prefiled Testimony, p. 16, ll. 13-15. Witness Bleiweis recommended that with regard to Pro Forma Plant only those projects that have begun and are expected to be completed shortly be recognized for ratemaking purposes. *Id.* at ll. 2-4. With regard to his proposed adjustment to CWIP,

Bleiweis recommended that only the one project expected to be completed shortly be recognized for ratemaking purposes. *Id.* at 4-6.

Staff witness Scott recommended an adjustment to Pro Forma Plant of \$23,239 for completed additions. Staff's adjustment consists of \$9,913 for a completed plant addition and \$13,326 transferred from CWIP. The \$9,913 for the completed plant is for the installation of diffused aeration at the Pocalla Water and Wastewater Treatment Plant. Scott Direct testimony, p. 13, ll.1-4. The \$13,326 transfer from CWIP is for an upgrade to the lift station in the River Hills Subdivision. *Id.* at ll. 4-6. According to witness Scott, Staff verified the total adjustment of \$23,239. *Id.* at l.2.

Upon consideration of this item, the Commission adopts the adjustment proposed by Staff. The Commission rejects the adjustment proposed by CWS because the adjustment does not reflect actual completed additions to plant but rather estimates of the plant projects under construction that are not yet completed. As the projects are not yet completed, those additions are not yet providing service and cannot be considered as used and useful in providing service. Therefore, the adjustment proposed by CWS does not meet with the standards of used and useful and known and measurable that would justify including the adjustment in the rate base.

Similarly, the Commission rejects the adjustment proposed by the Consumer Advocate. The adjustment proposed by the Consumer Advocate includes amounts for plant projects that are not yet completed. The Commission believes that the Pro Forma Plant should only include plant projects that have been completed and for which verification of the amount of plant is available. Those projects which are actually

completed and are used in providing service meet the used and useful standard. Likewise, projects whose costs can be determined and verified and whose costs are not mere estimates meet the known and measurable standard. Additionally, with the exception of \$13,326, the Consumer Advocate proposes an adjustment which eliminates the CWIP balance at December 31, 2000, from rate base. There is no evidence in the record to suggest that CWIP expenditures at the end of the test year were imprudently incurred or that they were not incurred on behalf of the ratepayer. In fact, an analysis of the CWIP balance at the end of the test year reveals that the expenditures were incurred for projects to improve service to existing ratepayers. The Commission, therefore, finds that CWIP is a proper component to be included in rate base and rejects the adjustment proposed by the Consumer Advocate.

(F) Water Service Rate Base:

(1) Position of CWS: CWS did not propose an adjustment to this item.

(2) Position of Staff: The Staff proposed an adjustment of (\$8,457) to adjust the WSC Rate Base. Staff verified the WSC rate base and removed deferred charges, adjusted accumulated deferred income taxes, and adjusted accumulated depreciation. Staff allocated WSC's rate base based upon updated customer equivalents for the total WSC Rate Base allocated to CWS of \$150,190. Staff's computed Rate Base of \$150,190 less the per book amount of \$158,647 results in an adjustment of (\$8,457).

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment to this item.

(4) Position of RHCA: RHCA did not propose an adjustment to this item.

(5) Decision of the Commission: In its adjustment, Staff proposes to remove (\$8,457) from the rate base to adjust the WSC rate base allocated to CWS. A portion of the rate base of WSC is allocated to CWS. During its audit, Staff verified the rate base of WSC to WSC's books and records. Witness Scott testified that Staff removed deferred charges of \$40,526 and adjusted Accumulated Deferred Income Taxes. Scott Direct Prefiled Testimony, p. 13. Using updated customer equivalents Staff allocated WSC's rate base and determined a total WSC Rate Base allocated to CWS of \$150,190. As per book WSC rate base amounted to \$158,647, and Staff removed (\$8,457).

Upon consideration of this adjustment, the Commission finds the basis and methodology utilized by Staff reasonable and appropriate. Therefore, the Commission adopts the adjustment proposed by Staff.

(G) CWS Building Lease to Bio Tech:

- (1) Position of CWS: CWS did not propose an adjustment for this item
- (2) Position of Staff: The Staff proposed to allocate a portion of CWS plant associated with the business office in West Columbia. Staff's adjustment reduced Plant in Service by (\$249,565) and decreased Accumulated Depreciation by \$111,471.
- (3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment for this item.
- (4) Position of RHCA: RHCA did not propose an adjustment for this item.
- (5) Decision of the Commission: Bio Tech, a sister company to CWS, shares the office building in West Columbia with CWS. CWS owns the building and has leased it to Bio Tech for five years for a total of \$5.00 for the term of the lease. Bio Tech occupies

51% or 4,400 square feet of the total 8,600 square foot building. To account for the sharing of the office building, Staff made adjustments to rate base. From Plant in Service, Staff removed 51% of the value of the office building of \$487,786, amounting to (\$249,565). Staff also removed 51% of Accumulated Depreciation of \$217,876, amounting to \$111,471.

The Commission finds the Staff's adjustment appropriate and hereby adopts that adjustment. The office building is not totally utilized by CWS. Therefore, the Commission finds it appropriate to remove from the Company's rate base that portion of the office building that does not benefit CWS. Rate base is the amount of investment on which a regulated utility is entitled to an opportunity to earn a fair and reasonable return ... [and] represents the total investment in, or the fair value of, the used and useful property which it necessarily devotes to rendering the regulated services. *See, Hamm v. South Carolina Public Service Commission*, 309 S.C. 282, 422 S.E.2d 110 (1992). Thus the portion of the office building not used by CWS cannot meet the standard that the investment be "used and useful" in rendering service to the regulated utility's customers.

(H) Plant Associated with Bulk Water Agreements:

(1) Position of CWS: CWS proposed that only the I-20 and Watergate water supply facilities should be removed from rate base. CWS maintains that the River Hills wells are maintained in emergency back-up status. CWS also asserts that for whatever portion of the Staff's adjustment that the Commission may adopt, that CWS is entitled to an extraordinary retirement expense to offset the removal of that plant from the rate base. CWS proposes an amortization period of ten years for extraordinary retirement expense.

CWS also proposes that it be allowed an out-of-test year adjustment for the interconnection of the Idlewood service area with the bulk supplier. CWS provided documentation at the hearing that the interconnection cost was \$22,223.

(2) Position of Staff: Staff proposed an adjustment of (\$288,119) to remove plant and accumulated depreciation expense associated with wells in River Hills, Watergate, and I-20 service areas which are no longer used and useful.

(3) Position of Consumer Advocate: The Consumer Advocate recommended an adjustment of \$288,119 to Net Plant in Service to remove the wells in the I-20, Watergate, and River Hills service areas which are receiving water through bulk water service agreements. The Consumer Advocate also recommended removal of wells from the Idlewood subdivision and the Westside Terrace subdivision.

(4) Position of RHCA: RHCA did not propose an adjustment for this item.

(5) Decision of the Commission: The Commission agrees that the adjustment proposed by the Staff and the Consumer Advocate of (\$288,119) to remove the wells in the I-20, Watergate, and River Hills service areas is an appropriate adjustment. The record is clear that these wells were not used during the test year as the customers in those service areas are receiving bulk water from a bulk water supplier. Therefore, the wells do not meet the “used and useful” standard for inclusion in rate base.

Further, the Commission finds it appropriate to remove the wells in the Idlewood and Westside Terrace service areas from the rate base. Removal of the Idlewood and Westside Terrace wells results in an adjustment of (\$11,118). The record establishes that the interconnection for bulk water was made for Idlewood to receive bulk water from a

bulk water supplier. Furthermore, the Company has submitted evidence in the form of invoices and bills showing that the interconnection has been completed at a cost of \$22,223. While this expenditure for the interconnection was completed after the test year, it is a known and measurable out-of-test year adjustment which should be allowed. In *Porter v. South Carolina Public Service Commission*, 328 S.C. 22, 493 S.E.2d 92 (1997), the Supreme Court of South Carolina stated “[w]e have approved the historical test year as a basis for calculating a utility’s rate base as long as adjustments are made for any known and measurable out-of-period changes in expenses, revenues, and investments that would materially alter the rate base.” The interconnection of the Idlewood service area was completed after the test year. The cost of the interconnection is known and measurable as evidenced by the bills and invoices submitted by CWS. It is only fair to allow recovery of the interconnection, when removing the costs of the wells from the rate base.

Further, the Commission finds it appropriate to allow extraordinary retirement of these wells that are removed from the rate base. The Commission finds that a ten-year amortization of this extraordinary retirement, as proposed by CWS, is an appropriate time in which to recover the expense. As the Commission has approved removal from rate base of wells totaling \$299,237, the Commission approves an adjustment for extraordinary retirement of \$29,924.

Additionally, witness Wenz stated that the wells in the River hills service area were being maintained as back-up in case of emergency. While the Commission has found that those wells should not be included in rate base for not meeting the used and

useful standard, the Commission is aware from the testimony of witnesses Wenz and Daniel that CWS could at some future time return those wells to active status. Therefore, the Commission directs CWS to notify this Commission in writing should any of the facilities which have been removed from rate base in this proceeding be brought back into service.

(I) Accumulated Depreciation:

(1) Position of CWS: CWS did not propose an adjustment for this item.

(2) Position of Staff: The Staff proposes to adjust accumulated depreciation to correspond to Staff's adjustment for annualized depreciation. Staff computed a reduction to depreciation expense of \$32,970. The Staff reduces Accumulated Depreciation by this amount.

(3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment for this item.

(4) Position of RHCA: RHCA did not propose an adjustment for this item.

(5) Decision of the Commission: Staff's adjustment to Accumulated Depreciation is the corresponding adjustment to the Staff's adjustment for annualized depreciation. As the Commission adopted the Staff's adjustment for annualized depreciation, it is appropriate to adopt the corresponding adjustment. The Commission therefore adopts the Staff adjustment and approves a decrease of \$32,970 to Accumulated Depreciation.

(J) Cash Working Capital:

(1) Position of CWS: CWS proposed an adjustment to Cash Working Capital of \$19,214 to adjust for pro forma adjustments to O&M Expenses, including Taxes Other Than Income.

(2) Position of Staff: Staff proposed an adjustment to Cash Working Capital of (\$6,051) to adjust for Staff's adjustments to O&M expenses which correct the per book operations.

(3) Position of Consumer Advocate: The Consumer Advocate proposed an adjustment of (\$98,288) to Cash Working Capital. The Consumer Advocate's adjustment was applied to recommended pro forma adjustments to O&M expenses only.

(4) Position of RHCA: RHCA made no adjustment for this item.

(5) Decision of the Commission: The adjustment proposed by CWS included Taxes Other Than Income in its computation. Neither the Staff nor the Consumer Advocate included Taxes Other Than Income in their respective adjustments to Cash Working Capital. Staff witness Scott stated that Staff does not include Taxes Other Than Income in Cash Working Capital because Taxes Other Than Income is normally an accrual not requiring a cash outlay and the Company would have collected funds from its customers in advance of paying certain taxes. Scott Direct testimony, p. 15. Consumer Advocate witness Bleiweis stated that Cash Working Capital represents the lag for O&M expenses only and should not be applied to Taxes Other Than Income. Bleiweis Direct Testimony, p. 22. All of the parties used a 12.5% factor in determining Cash Working Capital.

Upon consideration of this adjustment, the Commission adopts the method for the adjustment proposed by the Staff. The Commission agrees that a 12.5% factor should be applied to O&M expense only, exclusive of Taxes Other Than Income. The Cash Working Capital allowance represents an average expense lag time. As such, Cash Working Capital should only be applied to expenses adjusted for corrections and not to an accrual for which a cash outlay is not required before the funds are collected, as is the case of Taxes Other Than Income. The adjustment for Cash Working Capital based on the adjustments to O&M expenses for per book corrections for the test year approved in this Order will be (\$6,051).

(K) Customer Deposits:

- (1) Position of CWS: CWS did not propose an adjustment on this item.
- (2) Position of Staff: The Staff proposed to adjust for Interest on Customer Deposits. The Company booked accrued interest in a separate account, and Staff proposes to reduce Rate Base by the Interest of (\$219,269) owed to the customer.
- (3) Position of Consumer Advocate: The Consumer Advocate did not propose an adjustment for this item.
- (4) Position of RHCA: RHCA did not propose an adjustment for this item.
- (5) Decision of the Commission: The Staff adjustment to Interest on Customer Deposits would reduce rate base by (\$219,269). Staff's reasoning for this adjustment is that CWS booked accrued interest in a separate account and that this money is money owed to the customers. Upon consideration of the adjustment and the reasoning for the adjustment, the Commission adopts this adjustment. As the money is money owed to

customers as interest on the customer deposits, the money is money of the customers and not of CWS. Rate base is the amount of investment on which a regulated utility is entitled to an opportunity to earn a fair and reasonable return ... [and] represents the total investment in, or the fair value of, the used and useful property which it necessarily devotes to rendering the regulated services. *See, Hamm v. South Carolina Public Service Commission*, 309 S.C. 282, 422 S.E.2d 110 (1992). The interest on customer deposits does not represent an investment by the Company and is therefore not an item which should be included in the rate base.

Summary of Adopted Adjustments to Rate Base:

The total effect of the adjustments to rate base adopted herein reduce Gross Plant in Service by (\$546,232), decrease Accumulated Depreciation by \$144,440 [thereby resulting in a reduction to Net Plant in Service of (\$401,791), reduce CWIP by (\$13,326)], reduce Cash Working Capital by (\$6,051), reduce WSC rate base by (\$8,457), and increase Customer Deposits by (\$219,269). The total of the adjustments adopted herein reduce total rate base by (\$648,894). Thus, after the adjustments adopted herein, as adjusted rate base is \$11,464,268. The following table indicates the Company's rate base for its jurisdictional operations in South Carolina after accounting and pro forma adjustments approved herein:

TABLE C

Gross Plant in Service	\$31,070,694
LESS: Accumulated Depreciation	<u>(3,602,208)</u>
Net Plant in Service	27,468,487
ADD: Construction Work In Progress	182,910
Cash Working Capital	357,013
Water Service Corp. – Rate Base	150,190
DEDUCT: Advances in Aid of Construction	(1,000)
Contributions in Aid of Construction	(13,538,305)
Plant Acquisition Adjustment	(525,890)
Excess Book Value	(1,026,646)
Accumulated Deferred Income Taxes	(1,224,199)
Customer Deposits	<u>(378,291)</u>
TOTAL YEAR END RATE BASE	<u>\$11,464,268</u>

12. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 12

(1) Position of CWS: CWS did not propose a customer growth adjustment in its Application.

(2) Position of Staff: Staff computed customer growth as adjusted of \$7,903.

(3) Position of the Consumer Advocate: The Consumer Advocate proposed an adjustment for customer growth by applying the increase in the number of customers from December 31, 1999, to December 31, 2000, by average revenue per customer. The calculation resulted in an upward adjustment to revenue of \$40,196 and an upward-adjustment to income of \$39,839 after applying revenue related expenses.

(4) Position of RHCA: RHCA did not propose a specific growth adjustment to test year figures. RHCA proposed that tremendous growth in the Lake Wylie area of the Company's service territory provides sufficient future revenues to negate the need for a rate increase.

(5) Decision of the Commission: The Commission adopts the customer growth methodology as proposed by the Staff to include the adjustments adopted herein. Staff's adjustment is applied to Net Operating Income. As the Staff's customer growth adjustment is applied to Net Operating Income, the adjustment attributes an equal contribution to net income by each customer added. By applying the adjustment to Net Operating Income, Staff's customer growth adjustment recognizes growth in both revenues and expenses.

In *Porter v. South Carolina Public Service Commission*, 328 S.C. 222, 493 S.E.2d 92 (1997), the Supreme Court of South Carolina stated "adjustments for known and measurable changes in expenses are within the discretion of the Commission. Absolute precision is not required so long as adjustments are 'known and measurable' within a degree of reasonable certainty." The Commission finds that the Staff's adjustment for customer growth meets this definition as stated by the Supreme Court. Calculation of additional revenues from additional customers may be made quite easily. However, calculation of expenses associated with the addition of customers is not as straightforward. While it would be difficult to calculate the precise amount of expenses that the addition of one customer would add, it does not make sense to ignore expenses altogether when looking at customer growth. Some expenses may increase proportionally with the addition of customers while other expenses may not increase at a proportional rate. While the Staff's adjustment may not calculate increase in expenses with absolute precision, the Staff's adjustment, which is applied to Net Operating Income and which

therefore applies to both revenues and expenses, is a reasonable adjustment that comes with a “reasonable degree of certainty.”

The adjustment proposed by the Consumer Advocate only applies to revenues and not to expenses. The Commission believes that any adjustment for customer growth must necessarily also take into account increases in expenses. While it cannot be stated with absolute certainty that the addition of customers adds expenses in a directly proportionate manner, one cannot assume that the addition of customers does not increase expenses. This proposed adjustment only factors in one side of the equation (i.e. revenues) and ignores expenses. As noted above, while increases in expenses with the addition of customers may not be a proportional increase, one must not just ignore the increases in expenses. Therefore, the Commission rejects the customer growth adjustment proposed by the Consumer Advocate.

RHCA presented extensive testimony regarding projected growth in the River Hills service area. Witness Harrington testified to the opening of new residential developments within the Lake Wylie area that are within the service territory of CWS. Harrington also testified that the Lake Wylie area is experiencing tremendous growth due to the proximity of the Lake Wylie area to Charlotte, North Carolina and to improvements in access to the area. RHCA suggests that the tremendous growth in the Lake Wylie area of CWS’s service territory will provide sufficient income to CWS such that the requested rate increase is not needed.

While the testimony offered by RHCA does indeed suggest growth within the CWS service territory, the Commission cannot agree that such growth will obviate the

need for a rate increase. In establishing rates and a return for a utility, the Commission uses a historic test year, with appropriate adjustments made for known and measurable changes occurring outside the test year. *See, Heater of Seabrook, Inc. v. Public Service Commission of South Carolina*, 324 S.C. 56, 478 S.E.2d 826 (1996) (“when calculating expenses in rate cases, Commission should use only test year data and known and measurable changes occurring after the test year.”) The Commission must reject the proposal advanced by RHCA. First, the RHCA proposal does not consider the increase in expenses to the Company resulting from customer growth. While RHCA submitted calculations of additional revenues from projections of growth in the area, RHCA did not include any calculations as to the expenses that the Company will incur in providing service to those additional customers.

Further, the time period of the projected growth violates the known and measurable rule. Witness Harrington acknowledged on cross-examination that it was possible that some of the developments may not grow as quickly as anticipated by developers and further that a variety of factors could affect development. While the Commission has discretion to adjust for known and measurable changes or events and absolute precision in doing so is not required, such changes or events must be known and measurable within a degree of reasonable certainty for the Commission to exercise that discretion. *Porter, supra*. The Commission cannot say that the land use planning projections, which themselves involve projections regarding discretionary decision-making by third parties, over a four year period, as testified to by witness Harrington,

constitute an event that is known and measurable within a reasonable degree of certainty.

Thus the Commission rejects the customer growth proposal advanced by RHCA.

13. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 13

Under rate of return on rate base regulation, the Commission must approve an income requirement that will permit the Company to cover operating costs and provide an opportunity to earn the approved rate of return on the rate base. The determination of the income requirement requires a calculation using approved Operating Revenues and approved Operating Expenses to determine Net Operating Income for Return. Net Operating Income for Return is then increased for approved AFUDC and approved Customer Growth resulting in Total Income for Return. The following table illustrates the calculations of CWS's Total Income for Return:

TABLE D

	<u>After Increase</u>
Operating Revenues	\$5,295,379
Operating Expenses	<u>4,166,424</u>
Net Operating Income For Return	1,128,955
ADD: Allowance for Funds Used During Construction	14,602
Customer Growth	<u>9,718</u>
TOTAL INCOME FOR RETURN	<u>\$1,153,275</u>
Return on Rate Base	<u>10.06%</u>

As demonstrated on Table D, Total Income for Return after the increase approved herein is \$1,153,275.

14. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 14

In order for the Company to have the opportunity to earn the 10.06% rate of return on rate base approved herein, the Commission must increase revenues sufficient to

achieve a Total Income for Return of \$1,153,275, as calculated in Finding of fact No. 13. The additional revenue calculated for the Company to have the opportunity to earn its approved rate of return of 10.06% requires an increase of \$406,246.

15. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 15

Upon determination of the revenue requirements for a utility in a ratemaking proceeding, the next step is the determination of the specific rates or rate structure that will yield the required revenues. A generally accepted principle is that proper utility regulation requires the exercise of control over a utility's rate structure.

In designing rates for the Company, the Commission strives to set rates that are "just and reasonable" and without undue discrimination. In the case before the Commission, CWS has requested rates for the base facility charge for water service that result in a uniform water base facility charge. The Commission finds that such a uniform rate schedule is fair and reasonable and is in the best interests of the customers and CWS.

With regard to the rates for sewer service, CWS by its Application did not seek increases for those customers in the Lincolnshire service area, the I-20 service area, and the Lexington service area. The reasoning for this divergence in rates as expressed by CWS witness Wenz is that the status of the Company's operation and even its ownership of the systems serving those areas is in a state of flux. Those systems are operating under expired NPDES or ND permits and are either the subject of current or potential litigation. Due to those circumstances, witness Wenz testified that CWS felt that the uncertainty of the outcome of the issues involving those services areas led CWS not to seek rate relief for sewer treatment in those service areas.

At the night hearing in Summerville, customers of CWS testified that CWS was operating under expired NPDES permits in the Kings Grant service area. This fact is supported by Exhibit C to the Company's Application which indicates that the NPDES permit for Kings Grant expired in 1986. A review of Exhibit C to the Company's Application also reveals that Teal on Ashley is operating under an expired NPDES permit; that permit having expired in 2000. Further, testimony from the night hearing in Summerville indicated that the sewer plants from the Kings Grant service area and the Teal on Ashley service area are part of a 208 plan.

The justification from CWS for excluding the sewer customers in the I-20 service area, Lexington service area, and Lincolnshire service area appears to this Commission to be the same or similar circumstances as exist for those customers in the Kings Grant service area and the Teal on the Ashley service area. The Commission, therefore, finds it appropriate to exclude the customers in the Kings Grant service area and the Teal on the Ashley service area from the sewer rate increase.

16. EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 16

S.C. Code Ann. Section 5-240(H) (Supp.2000) provides, in part, that "[t]he [C]ommission shall specify an allowable operating margin in all water and wastewater orders." Based upon the rate of return on rate base approved herein and the revenues and expenses also approved herein, the corresponding operating margin is calculated to be 12.43%. The following Table reflects an operating margin of 12.43%:

TABLE E

Operating Revenues	\$5,295,379
Operating Expenses	<u>4,166,424</u>
Net Operating Income	\$1,128,955
ADD: Allowance for Funds Used During Construction	14,602
Customer Growth	<u>9,718</u>
Total Income for Return	<u>\$1,153,275</u>
Operating Margin (After Interest Expense of \$494,999)	<u>12.43%</u>

IV. CONCLUSIONS OF LAW

Based upon the Findings of Fact as contained herein and the record of the instant proceeding, the Commission makes the following Conclusions of Law:⁹

1. Rate of return on rate base is the appropriate guide for the Commission to use in determining the lawfulness of the rates of CWS and in fixing of just and reasonable rates for CWS to charge its customers in South Carolina.

2. A fair rate of return on rate base for the operation of CWS in South Carolina is 10.06%. This rate of return is calculated using a capital structure of 50.09% long-term debt and 49.91% equity, a cost of debt of 8.62%, and a return on equity of 11.50%. Based on the discussion and analysis of the Commission as detailed in this Order, these components of capital structure, cost of debt, and cost of equity and the resulting rate of return on rate base produce a fair and reasonable rate of return which the Company should have the opportunity to earn.

⁹ The Commission's analyses which give rise to the Conclusions of Law are contained in the discussions of Section III of this Order.

3. For the test year of December 31, 2000, the appropriate operating revenues, under present rates and as adjusted in this Order, are \$4,891,487, and the appropriate operating expenses, under present rates and as adjusted in this Order, are \$4,012,749.

4. Using the rate base as adjusted in this Order of \$11,464,268 and the return on rate base of 10.06% found to be fair and reasonable in this Order, the income requirement for CWS is \$1,153,275.

5. In order for CWS to have an opportunity to earn the return on rate base found reasonable and approved in this Order and to meet the income requirement, CWS must be allowed additional revenues of \$406,246.

6. The rates approved in this Order are designed to be just and reasonable without undue discrimination and are also designed to meet the revenue requirements of the Company.

7. Based on the adjustments approved herein and the increase in rates approved herein, the appropriate operating margin for CWS on its South Carolina operations is 12.43%.

IT IS THEREFORE ORDERED THAT:

1. CWS is granted a rate of return on rate base for its water and sewer operations in South Carolina of 10.06%.

2. The schedule of rates and charges attached hereto as Appendix A are hereby approved for service rendered on or after the date of this Order. Further, the

schedules are deemed to be filed with the Commission pursuant to S.C. Code Ann. Section 58-5-240 (Supp. 2000).

3. Should the schedules approved herein and attached hereto as Appendix A not be placed in effect until three (3) months from the effective date of this Order, the schedules shall not be charged without written permission from the Commission.

4. Should any of the facilities which have been removed from rate base in this proceeding be brought back into service by CWS at any time, CWS is required to provide written notice to the Commission that the removed facilities are back in service.

5. CWS shall maintain its books and records for water and sewer operations in accordance with the NARUC Uniform System of Accounts for Class B Water and Sewer Utilities, as adopted by this Commission.

6. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

Chairman

ATTEST:

Executive Director

(SEAL)

APPENDIX A

CAROLINA WATER SERVICE, INC.

FILED PURSUANT TO DOCKET NO. 2000 -207-W/S – ORDER NO 2001- 887
EFFECTIVE DATE: AUGUST 27, 2001

SCHEDULE OF RATES AND CHARGES

WATER

1. Monthly Charges

Residential

Base Facilities Charge - Residential

Monthly charge per single family
house, condominium, mobile home
or apartment unit:

\$10.00 per unit

Commodity Charge:

\$3.24 per 1,000
gallons or 134 cft

Commercial

5/8" meter	\$ 10.00
1" ◦	\$ 25.00
1.5" ◦	\$ 50.00
2" ◦	\$ 80.00
3" ◦	\$160.00
4" ◦	\$250.00

Commodity Charge:

\$3.24 per 1,000
gallons or 134 cft

2. Charge for Water Distribution Only

Where water is purchased from a government body or agency or other entity for
distribution and resale by the Company, the following rates apply:

Residential

Base facilities Charge - Residential

Monthly charge per single family
house, condominium, mobile home
or apartment unit:

\$10.00 per unit

Commodity charge:

\$1.85 per 1,000
gallons or 134 cft

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by meter size.

Commodity charge: \$1.85 per 1,000
gallons or 134 cft

A) Water Service Connection (New connections only)	\$300 per SFE*
B) Plant Impact Fee (New connections only)	\$400 per SFE*

4. Account Set-Up and Reconnection Charges

- a. Customer Account Charge - for new customers only.

All Areas	\$ 13.50
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b. Reconnection Charges: In addition to any other charges that may be due, a reconnection fee of thirty five dollars (\$35.00) shall be due prior to the Utility reconnecting service which has been disconnected for any reason set forth in Commission Rule R.103-732.5. Customers who ask to be reconnected within nine months of disconnection will be charged the monthly base facility charge for the service period they were disconnected. The reconnection fee shall also be due prior to reconnection if water service has been disconnected at the request of the customer.

5. Billing Cycle

Recurring charges will be billed monthly in arrears. Nonrecurring charges will be billed and collected in advance of service being provided.

6. Extension of Utility Service Lines and Mains

The Utility shall have no obligation at its expense to extend its utility service lines or mains in order to permit any customer to connect to its water system. However, anyone or any entity which is willing to pay all costs associated with extending an appropriately sized and constructed main or utility service line from his/her/its premises to any appropriate connection point, to pay the appropriate fees and charges set forth in this rate schedule, and comply with the guidelines and standards hereof, shall not be denied service, unless water supply is unavailable or unless the South Carolina Department of Health and Environmental Control or other government entity has restricted the Utility from adding for any reason additional customers to the serving water system. In no event will the Utility be required to construct additional water supply capacity to serve any customer or entity without an agreement acceptable to the Utility first having been reached for the payment of all costs associated with adding water supply capacity to the affected water system.

* A Single Family Equivalent (SFE) shall be determined by using the South Carolina Department of Environmental Control Guidelines for Unit Contributory Loadings for Domestic Wastewater Treatment Facilities -- 25 S.C. Code Ann. Regs. 61-67 Appendix A (2000 Supp.)

SCHEDULE OF RATES AND CHARGES

SEWER

1. Monthly Charges

Residential - monthly charge per single-family house, condominium, villa, or apartment unit:	\$30.33 per unit
Mobile Homes - monthly charge:	\$22.75 per unit
Commercial - monthly charge:	\$30.33 per SFE*

Lincolnshire, I-20, Watergate, Kings Grant and Teal-on-the-Ashley areas

Residential - monthly charge per single-family house, condominium, villa, or, apartment unit:	\$28.86 per unit
Mobile Homes - monthly charge:	\$21.64 per unit
Commercial - monthly charge:	\$28.86 per SFE*

Commercial customers are those not included in the residential category above and include, but are not limited to, hotels, stores, restaurants, offices, industry, etc.

Charge for Sewage Collection Service Only (All Areas)

When sewage is collected by the Utility and transferred to a government body or agency, or other entity, for treatment, the Utility's rates are as follows:

Residential - monthly charge per single-family house, condominium, or apartment unit	\$19.38 per unit
Commercial - monthly charge per single-family equivalent	\$19.38 per SFE*

The Utility will also charge for treatment services provided by the government body or agency, or other entity. The rates imposed or charged by the government body or agency, or other, entity providing treatment will be charged to the Utility's affected customers on a pro rata basis, without markup. Where the Utility is required under the terms of the 201/208 Plan to interconnect to the sewage treatment system of a government body or agency or other entity and tap/connection/impact fees are imposed by that entity, such tap/connection/impact fees will be charged to the Utility's affected customers on a pro rata basis, without markup.

Solids Interceptor Tanks

For all customers receiving sewage collection service through an approved solids interceptor tank, the following additional charges shall apply:

A. Pumping Charge

At such time as the Utility determines through its inspection that excessive solids have accumulated in the interceptor tank, the Utility will arrange for pumping the tank and will include \$150.00 as a separate item in the next regular billing to the customer.

B. Pump Repair or Replacement Charge

If a separate pump is required to transport the customer's sewage from solids interceptor tank to the Utility's sewage collection system, the Utility will arrange to have this pump repaired or replaced as required and will include the cost of such repair or replacement and may be paid for over a one year period.

C. Visual Inspection Port

In order for a customer who uses a solids interceptor tank to receive sewage service from the Utility or to continue to receive such service, the customer shall install at the customer's expense a visual inspection port which will allow for observation of the contents of the solids interceptor tank and extraction of test samples therefrom. Failure to provide such a visual inspection port after timely notice of not less than thirty (30) days shall be just cause for interruption of service until a visual inspection port has been installed.

2. Nonrecurring Charges

- | | |
|--|----------------|
| A) Sewer Service Connection (New connections only) | \$300 per SFE* |
| B) Plant Impact Fee (New connections only) | \$400 per SFE* |

The nonrecurring charges listed above are minimum charges and apply even if the equivalency rating of a non residential customer is less than one (1). If the equivalency rating of a non residential customer is greater than one (1), then the

proper charge may be obtained by multiplying the equivalency rating by the appropriate fee. These charges apply and are due at the time new service is applied for, or at the time connection to the sewer system is requested.

3. Notification, Account Set-Up and Reconnection Charges

a. Notification Fee

A fee of four dollars (\$4.00) shall be charged each customer to whom the Utility mails the notice as required by Commission Rule R. 103-535.1 prior to service being discontinued. This fee assesses a portion of the clerical and mailing costs of such notices to the customers creating the cost.

b. Customer Account Charge - for new customers only.

All Areas	\$ 13.50
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A one-time fee to defray the costs of initiating service. This charge will be waived if the customer also takes water service.

- c. Reconnection Charges: In addition to any other charges that may be due, a reconnection fee of two hundred fifty dollars (\$250.00) shall be due prior to the Utility reconnecting service which has been disconnected for any reason set forth in Commission Rule R.103-532.4. Where an elder valve has been previously installed, a reconnection charge of thirty-five dollars (\$35.00) shall be due. Customers who ask to be reconnected within nine months of disconnection will be charged the monthly service charge for the service period they were disconnected.

4. Billing Cycle

Recurring charges will be billed monthly, in arrears. Nonrecurring charges will be billed and collected in advance of service being provided.

5. Toxic and Pretreatment Effluent Guidelines

The Utility will not accept or treat any substance or material that has been defined by the United States Environmental Protection Agency ("EPA") or the South Carolina Department of Environmental Control ("DHEC") as a toxic pollutant, hazardous waste, or hazardous substance, including pollutants falling within the provisions of 40 CFR 5129.4 and 401.15. Additionally, pollutants or pollutant properties subject to 40 CFR 5403.5 and 403.6 are to be processed according to the pretreatment standards applicable to such pollutants or pollutant properties, and such standards constitute

the Utility's minimum pretreatment standards. Any person or entity introducing any such prohibited or untreated materials into the Company's sewer system may have service interrupted without notice until such discharges cease, and shall be liable to the Utility for all damages and costs, including reasonable attorney's fees, incurred by the Utility as a result thereof.

6. Extension of Utility Service Lines and Mains

The Utility shall have no obligation at its expense to extend its utility service lines or mains in order to permit any customer to discharge acceptable wastewater into one of its sewer systems. However, anyone or any entity which is willing to pay all costs associated with extending an appropriately sized and constructed main or utility service line from his/her/its premises to an appropriate connection point, to pay the appropriate fees and charges set forth in this rate schedule and to comply with the guidelines and standards hereof, shall not be denied service, unless treatment capacity is unavailable or unless the South Carolina Department of Health and Environmental Control or other government entity has restricted the Utility from adding for any reason additional customers to the serving sewer system.

In no event will the Utility be required to construct additional wastewater treatment capacity to serve any customer or entity without an agreement acceptable to the Utility first having been reached for the payment of all costs associated with adding wastewater treatment capacity to the affected sewer system.

* A Single Family Equivalent (SFE) shall be determined by using the South Carolina Department of Environmental Control Guidelines for Unit Contributory Loading for Domestic Wastewater Treatment Facilities --25 S.C. Code Ann. Regs. 61-67 Appendix A (2000 Supp.) Where applicable, such guidelines shall be used for determination of the appropriate monthly service and tap fee.